

# Auditing Procedures Report

Issued under P.A. 2 of 1968, as amended.

Local Government Type <input checked="" type="checkbox"/> City <input type="checkbox"/> Township <input type="checkbox"/> Village <input type="checkbox"/> Other		Local Government Name <b>City of Muskegon Heights</b>	County <b>Muskegon</b>
Audit Date <b>12/31/04</b>	Opinion Date <b>6/28/05</b>	Date Accountant Report Submitted to State: <b>7/6/05</b>	

We have audited the financial statements of this local unit of government and rendered an opinion on financial statements prepared in accordance with the Statements of the Governmental Accounting Standards Board (GASB) and the *Uniform Reporting Format for Financial Statements for Counties and Local Units of Government in Michigan* by the Michigan Department of Treasury.

We affirm that:

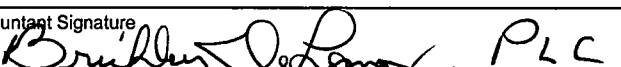
1. We have complied with the *Bulletin for the Audits of Local Units of Government in Michigan* as revised.
2. We are certified public accountants registered to practice in Michigan.

We further affirm the following. "Yes" responses have been disclosed in the financial statements, including the notes, or in the report of comments and recommendations

You must check the applicable box for each item below.

- ☐ Yes ☒ No 1. Certain component units/funds/agencies of the local unit are excluded from the financial statements.
- ☒ Yes ☐ No 2. There are accumulated deficits in one or more of this unit's unreserved fund balances/retained earnings (P.A. 275 of 1980).
- ☒ Yes ☐ No 3. There are instances of non-compliance with the Uniform Accounting and Budgeting Act (P.A. 2 of 1968, as amended).
- ☐ Yes ☒ No 4. The local unit has violated the conditions of either an order issued under the Municipal Finance Act or its requirements, or an order issued under the Emergency Municipal Loan Act.
- ☐ Yes ☒ No 5. The local unit holds deposits/investments which do not comply with statutory requirements. (P.A. 20 of 1943, as amended [MCL 129.91], or P.A. 55 of 1982, as amended [MCL 38.1132]).
- ☒ Yes ☐ No 6. The local unit has been delinquent in distributing tax revenues that were collected for another taxing unit.
- ☐ Yes ☒ No 7. The local unit has violated the Constitutional requirement (Article 9, Section 24) to fund current year earned pension benefits (normal costs) in the current year. If the plan is more than 100% funded and the overfunding credits are more than the normal cost requirement, no contributions are due (paid during the year).
- ☐ Yes ☒ No 8. The local unit uses credit cards and has not adopted an applicable policy as required by P.A. 266 of 1995 (MCL 129.241).
- ☐ Yes ☒ No 9. The local unit has not adopted an investment policy as required by P.A. 196 of 1997 (MCL 129.95).

We have enclosed the following:	Enclosed	To Be Forwarded	Not Required
The letter of comments and recommendations.	✓		
Reports on individual federal financial assistance programs (program audits).			✓
Single Audit Reports (ASLGU).	✓		

Certified Public Accountant (Firm Name) <b>Brickley Delong, PLC</b>			
Street Address <b>500 Terrace Plaza</b>	City <b>Muskegon</b>	State <b>MI</b>	ZIP <b>49443</b>
Accountant Signature 		Date <b>7/6/05</b>	

City of Muskegon Heights  
Muskegon County, Michigan

**REPORT ON FINANCIAL STATEMENTS**  
(with required supplementary information)

Year ended December 31, 2004

City of Muskegon Heights  
**LIST OF ELECTED AND APPOINTED OFFICIALS**  
December 31, 2004

**ELECTED OFFICIALS**

Mayor ..... Rillastine Wilkins

Mayor Pro Tem ..... Willie Burrell

City Council..... Keith Guy  
Dorothy Scott  
Darrell Paige  
Jackie Darnell  
Kimberley Sims

**APPOINTED OFFICIALS**

City Manager ..... Melvin C. Burns, II

City Clerk ..... Betty Ivory

Finance Director..... Lori Doody

City Assessor/Treasurer/Income Tax  
Administrator ..... Robert Jackson

# City of Muskegon Heights

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As management of the City of Muskegon Heights, we present to the readers of the City's financial statements this overview and analysis of the financial activities of the City of Muskegon Heights for the fiscal year ended December 31, 2004. We encourage you to consider the information presented in these financial statements along with the additional information that has been furnished in this letter. To those familiar with prior year financial statements or just new to this document, it is important to know that this is only the second year the City of Muskegon Heights is presenting this analysis along with these statements in a new format prescribed by the provisions of the Governmental Accounting Standards Board Statement 34 (GASB 34).

### FINANCIAL HIGHLIGHTS

- The City of Muskegon Heights issued \$1.5 million in Fiscal Stabilization Bonds
- City Council approved two additional operating mills for the City's General Fund.
- The fund balance for Other Governmental Funds increased from \$351,531 in 2003 to \$598,059 in 2004.
- The City's Major Street Fund is on track with its deficit elimination plan. The Fund deficit decreased from \$365,761, in 2003 to \$150,402, in 2004.

### OVERVIEW OF THE FINANCIAL STATEMENTS

The discussion and analysis is intended to serve as an introduction to the City's basic financial statements. The City's basic financial statements are comprised of three components: 1) governmental-wide financial statements, 2) fund financial statements and 3) notes to the financial statements. This report also contains other supplementary information in addition to the basic financial statements themselves.

#### Government-wide Financial Statements

The government-wide financial statements are designed to provide the reader with a broad overview of the City's finances. These statements are similar to those of a private sector business.

The Statement of Net Assets presents information on all of the City's assets and liabilities, with the difference between the two reported as net assets. Over time, increases or decreases in net assets may serve as a useful indicator of whether the financial position of the City is improving or deteriorating. The Statement of Activities presents information showing how the City's net assets changed during the fiscal year. All changes in net assets are reported when the event giving rise to the change occurs, regardless of the timing of related cash flows. Thus, revenues and expenses are reported in this statement for some items that will only result in cash flows in the future fiscal periods.

Both of the government-wide financial statements mentioned above distinguish functions of the City that are principally supported by taxes and intergovernmental revenues (governmental activities) from other functions that are designed to recover all or a significant part of their costs through user fees and charges for services (business-type activities). The governmental activities of the City of Muskegon Heights include general government, public safety, public works, community and economic development, and cultural and recreational activities. The business-type activities of the City include water distribution, water filtration and sewer services.

The government-wide financial statements include not only the City of Muskegon Heights (the primary government) but also the legally separate Muskegon Heights Downtown Development Authority. The board of this organization is appointed by the City and given the interrelation of the two, there is some potential liability for the City due to the City's pledge of its full faith and credit for debt obligations. The financial information of this component unit is reported in a separate column from the financial information of the primary government itself.

**Fund Financial Statements.** A fund is a grouping of related accounts that is used to maintain control over resources that have been segregated for specific activities or objectives. The City of Muskegon Heights, like other state and local governments, uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements. All of the funds of the City can be divided into three categories-governmental funds, proprietary funds and fiduciary funds.

**Governmental Funds.** Governmental funds are used to account for essentially the same functions reported as governmental activities in the government-wide financial statements. However, unlike the government-wide financial statements, governmental fund financial statements focus on current sources and uses of spendable resources, as well as on balances of spendable resources available at the end of the fiscal year. This information may be useful in evaluating a governmental entity's short-term financing requirements.

Because the focus of governmental funds is narrower than that of the government-wide financial statements, it is useful to compare the information presented for governmental funds with similar information presented for governmental activities in the government-wide financial statements. By doing so, readers may better understand the long-term impact of the government's short-term financing decisions. Both the governmental fund balance sheet and the governmental fund statement of revenues, expenditures, and changes in fund balances provide a reconciliation to facilitate this comparison between the two.

The City of Muskegon Heights maintains more than a dozen individual governmental funds. Information is presented separately in the governmental fund balance sheet and in the governmental fund statement of revenues, expenditures and changes in fund balances for the General Fund, which is considered a major fund. Data from the other funds are combined into a single, aggregated presentation. Individual fund data for each of these non-major governmental funds is provided in the form of combining statements elsewhere in this report.

**Proprietary Funds.** The City of Muskegon Heights has one type of proprietary fund. Enterprise funds are used to report the same functions presented as business-type activities in the government-wide financial statements. The City uses enterprise funds to account for its water distribution, water filtration and sewer services.

Enterprise funds provide the same type of information as the government-wide financial statements, only in more detail. The enterprise funds financial statements provided separate information for Water, Water Supply and Sewer funds all of which are major funds.

**Fiduciary Funds.** Fiduciary Funds are used to account for resources held for the benefit of parties outside the City. Fiduciary funds are not reflected on the government-wide financial statements because the resources from those funds are not available to support the City's programs. The accounting method used for fiduciary funds is much like that used for the proprietary funds.

**Notes to the Financial Statements.** The notes provide additional information that is essential to a full understanding of the data provided in the government-wide and fund financial statements. The reader is encouraged to include the reading of this section in any attempt to analyze and understand these statements.

**Other Information.** In addition to the basic financial statements and accompanying notes, this report also presents certain required supplementary information concerning the City's budgetary information as it relates to the actual expenditures for the General Fund.

### **Government-wide Financial Analysis**

The first table presented below is a summary of the government-wide statement of net assets for the City of Muskegon Heights. As stated earlier, the net assets may be used as an indicator of a government's financial health. As of December 31, 2004, the City's net assets from governmental activities totaled \$8,905,839 (45%) and \$10,956,564 (55%) from business-type activities, creating a total government-wide net assets total of \$19,862,403. The City's total net assets decreased 3.6% from 2003 to 2004. The overall net assets decrease was primarily due to the depreciation of the City's infrastructure.

In examining the composition of these net assets, the reader should note that governmental activities net assets are invested in capital assets (i.e., streets, buildings, land, vehicles, equipment, etc.) These assets are used to provide services to the City's residents, and they are not available to pay salaries, operational expenses or fund capital projects. The unrestricted net assets for governmental-type activities' depict a deficit of \$1,319,489 in 2003. As of December 31, 2004, that amount had increased by \$156,724 to \$1,476,213.

Business-type activities continue to have positive fund balances, which are represented as unrestricted net assets. The total for unrestricted net assets for business-type activities in 2004 was \$3,039,958, representing 28% of total net assets. In 2003, the total was \$3,225,570, which accounted for 28% of unrestricted net assets. The Sewer Fund's unrestricted net assets decreased approximately 5% in 2004 to \$1,441,301. The Water Fund, which had a deficit of \$359,587 at the close of 2003, decreased its deficit in 2004 to \$219,686. The Water Supply Fund still maintains a healthy balance, despite its decrease from \$2,067,843 to \$1,882,343.

### City of Muskegon Heights Net Assets

	Governmental Activities		Business-type Activities		Total	
	<u>2004</u>	<u>2003</u>	<u>2004</u>	<u>2003</u>	<u>2004</u>	<u>2003</u>
Current assets and other assets	\$ 2,479,076	\$ 1,114,777	\$ 3,105,847	\$ 3,292,238	\$ 5,584,923	\$ 4,407,015
Noncurrent assets	10,555,234	11,113,360	26,528,954	27,254,512	37,084,188	38,367,872
Total assets	13,034,310	12,228,137	29,634,801	30,546,750	42,669,111	42,774,887
Current liabilities	1,615,205	1,700,962	1,283,736	1,324,543	2,898,941	3,025,505
Noncurrent liabilities	2,513,266	1,226,010	17,394,501	17,813,799	19,907,767	19,039,809
Total liabilities	4,128,471	2,926,972	18,678,237	19,138,342	22,806,708	22,065,314
Net assets						
Invested in capital assets,						
net of related debt	9,669,899	10,128,549	6,002,660	6,350,924	15,672,559	16,479,473
Restricted	712,153	492,105	1,849,946	1,831,914	2,562,099	2,324,019
Unrestricted	(1,476,213)	(1,319,489)	3,103,958	3,225,570	1,627,745	1,906,081
Total net assets	\$ 8,905,839	\$ 9,301,165	\$ 10,956,564	\$ 11,408,408	\$ 19,862,403	\$ 20,709,573

**Governmental Activities.** Governmental activities net assets decreased by \$550,644 or 6% during the 2004 fiscal year. With all of the City's governmental operations combined, the net result was that its operating revenues were exceeded by its operating expenditures, producing the resulting deficit. The following table depicts this occurrence which will be discussed in more detail later in this analysis.

**Business-type Activities.** Total net asset for business-type activities decreased from \$11,408,408 in 2003 to \$10,956,564 in 2004. This is a decrease of approximately 4%. The major cause for this decrease can be found in the increase in depreciation for the year. The Water Supply Fund, which is a component of the business-type activity, experienced its first full year of depreciation costs related to the water filtration plant expansion and improvement project that began in 2000. There was also a new high service pumping station added to the system that experienced its first full year of depreciation costs.



## City of Muskegon Heights Changes in Net Assets

	Governmental Activities		Business-type Activities		Total	
	<u>2004</u>	<u>2003</u>	<u>2004</u>	<u>2003</u>	<u>2004</u>	<u>2003</u>
Revenues:						
Program revenues						
Charges for services	\$ 862,695	\$ 786,005	\$ 4,285,584	\$ 4,205,219	\$ 5,148,279	\$ 4,991,224
Operating grants	1,880,592	613,933	-	-	1,880,592	613,933
Capital grants and contributions	462,938	-	-	522,393	462,938	522,393
General revenues						
Property taxes	1,961,330	1,894,774	-	-	1,961,330	1,894,774
Income taxes	1,020,227	926,666	-	-	1,020,227	926,666
Franchise taxes	91,874	94,467	-	-	91,874	94,467
Grants and contributions not restricted	1,926,545	2,816,307	-	-	1,926,545	2,816,307
Unrestricted investment earnings	39,005	23,320	100,550	30,040	139,555	53,360
Miscellaneous	137,505	458,989	-	-	137,505	458,989
Gain on sale of assets	(21,423)	13,613	-	-	(21,423)	13,613
Total revenues	<u>8,361,288</u>	<u>7,628,074</u>	<u>4,386,134</u>	<u>4,757,652</u>	<u>12,747,422</u>	<u>12,385,726</u>
Expenses:						
General government	2,174,833	2,173,500	-	-	2,174,833	2,173,500
Public safety	3,376,259	3,373,245	-	-	3,376,259	3,373,245
Public works	2,266,537	2,303,921	-	-	2,266,537	2,303,921
Community and economic development	744,461	503,109	-	-	744,461	503,109
Culture and recreation	314,126	269,074	-	-	314,126	269,074
Interest on long-term debt	59,984	61,490	-	-	59,984	61,490
Sewer Fund	-	-	792,153	817,480	792,153	817,480
Water Fund	-	-	1,225,426	1,330,505	1,225,426	1,330,505
Water Supply Fund	-	-	2,796,131	1,859,947	2,796,131	1,859,947
Total expenses	<u>8,936,200</u>	<u>8,684,339</u>	<u>4,813,710</u>	<u>4,007,932</u>	<u>13,749,910</u>	<u>12,692,271</u>
Change in net assets before transfers	(574,912)	(1,056,265)	(427,576)	749,720	(1,002,488)	(306,545)
Transfers	24,268	25,399	(24,268)	(25,399)	-	-
Change in net assets	(550,644)	(1,030,866)	(451,844)	724,321	(1,002,488)	(306,545)
Net assets - at beginning of year	9,456,483	10,332,031	11,408,408	10,684,087	20,864,891	21,016,118
Net assets - end of year	<u>\$ 8,905,839</u>	<u>\$ 9,301,165</u>	<u>\$ 10,956,564</u>	<u>\$ 11,408,408</u>	<u>\$ 19,862,403</u>	<u>\$ 20,709,573</u>

**Financial analysis of the Government's Funds**

As stated earlier in this discussion and analysis, the City of Muskegon Heights uses fund accounting to ensure and demonstrate compliance with finance-related legal requirements.

**Governmental funds.** The focus of the City of Muskegon Heights governmental funds is to provide information on near-term inflows, outflows, and balances in spendable resources. Such information is useful in assessing the City's financing requirements. In particular, unreserved fund balances or the lack thereof, may serve as a useful measure of a government's net resources available for spending at the end of the fiscal year.

At the end of the 2004 fiscal year, the City of Muskegon Heights governmental funds reported a combined unreserved fund balance of \$297,348. This total unreserved fund balance is comprised of the General Fund balance of \$226,673 and \$70,675 in other governmental funds. It is necessary to further distinguish between the unreserved and reserved fund balance. The unreserved balance represents what is available for spending at the City's discretion. The remainder of the fund balance is reserved to indicate that it is not available for new spending because it has already been committed to 1) liquidate contracts and purchase orders (\$152,223), 2) pay debt service and capital purchase (\$30,260), and 3) reserves for cemetery perpetual care (\$497,124). When the fund balance has been adjusted to account for these reserves, the result is a total fund balance of \$976,955, which consists of a balance of \$378,896 in the General Fund a fund balance of \$598,059 in other governmental funds.

The General Fund is the chief operating fund of the City of Muskegon Heights. At the end of the 2003 fiscal year, the unreserved General Fund deficit was \$1,032,958 and the total General Fund deficit was \$938,843. At the end of 2004, The General Fund had a positive to fund balances of \$226,673 and \$378,896 respectively. In December of 2004, the City of Muskegon Heights issued \$1,500,000 Limited Tax Obligation fiscal Stabilization Bonds. The purpose of these bonds was to pay off the City's lingering debts and eliminate its operating deficit.

The other governmental funds column consists of various funds. The Major Street Fund is the largest fund in that schedule. The Major Street Fund improved its fund equity by \$215,359, which reduced the end of year fund deficit to \$150,402. As part of a multi-year deficit elimination plan, the City did not participate in any major infrastructure projects in 2003 or 2004. The plan also called for the reduction of full-time employees and other cost cutting measures.

**Proprietary funds.** The City of Muskegon Heights proprietary funds provide the same type of information found in the governmental financial statements, but in more detail. Net assets of the Sewer Fund decreased by \$30,300. Although the operating revenues of this fund exceed the operating expenses, once the \$75,221 non-operating expense of interest payments was included, the result was a decrease in net assets. The net assets of the Water Fund increased by \$86,320 primarily due to a rate adjustment implemented by the City Council in April of 2004. The Water Supply Fund's net assets decreased by \$507,864 in 2004. The Water Supply Fund's depreciation expenses increase by 75% and interest expense increased by over 100%, thus resulting in the approximately 6% decrease in its net assets. As stated above, the net assets of the three proprietary funds combined, decreased 4%, from \$11,408,408 in 2003 to \$10,956,564 in 2004.

**General Fund Budget**

During the current fiscal year, the City made several amendments to its original budget. The most significant of those is listed below:

- Increased revenue by approximately \$1.44 million for fiscal stabilization bond proceeds.
- City attorney was increased by \$45,000. The City negotiated six of its seven labor contracts with the assistance of the city attorney in 2004. These negotiations resulted in increased costs.
- Other general government expenses were increased due to a larger than expected increase in health insurance costs.
- Taxes were reduced due to a drop income tax collection of approximately 5% due to overall economic conditions.
- Various other adjustments were made during the year related to normal fluctuations in actual costs incurred.
- Capital outlay budget was amended for a FEMA grant.

The following comments summarize the major variations from the final budget to actual revenues and expenditures.

- Intergovernmental revenues were 3% less than budgeted due to the economic climate. This included a 5% governor mandated decrease in state shared revenue.
- Police department had expenditures 6% below its final budget. This was due to the increased use of part-time employees.
- The costs for refuse collection has been less than budgeted due to declines in population and restrictions on items that can be collected.
- Debt service was overbudget due to the reclassification of lease payments for police cruisers to debt service.
- Capital outlay was over budget due to the acquisition of a police cruiser acquired with grant funds and some capital outlay items being included as part of the total department budget.

**Capital Assets Administration**

**Capital Assets.** The City of Muskegon Heights investment in capital assets for its governmental and business-type activities was \$34,173,621 (net of accumulated depreciation) at the close of 2003. In 2004, this total decreased approximately 4% to \$32,822,580. The investment in capital assets includes land, buildings, infrastructure, improvements, machinery, equipment, plants, and vehicles.

Major capital asset events during the current fiscal year included the following:

- \$16,500 in land was added, and \$10,000 in land was sold in governmental type activities. These were primarily tax-reverted buildings and land.
- Furniture and equipment had new additions of \$436,739 related to new traffic signals and fire equipment.
- In 2003 the depreciation expense for all business type activity was \$489,304, in 2004 that amount increased to \$815,364 due to increases in assets at in the Water Supply Fund.

**City of Muskegon Heights Capital Assets  
(Net of Accumulated Depreciation)**

	Governmental Activities		Business-type Activities		Total	
	2004	2003	2004	2003	2004	2003
Land	\$ 254,408	\$ 247,908	\$ 40,012	\$ 40,012	\$ 294,420	\$ 287,920
Buildings and improvements	692,665	677,435	-	-	692,665	677,435
Infrastructure	7,652,085	8,545,277	-	-	7,652,085	8,545,277
Plants and infrastructure	-	-	22,255,170	22,978,250	22,255,170	22,978,250
Furniture and equipment	881,700	513,052	-	-	881,700	513,052
Machinery and equipment	-	-	28,747	51,105	28,747	51,105
Vehicles	1,017,793	1,120,582	-	-	1,017,793	1,120,582
Total	<u>\$ 10,498,651</u>	<u>\$ 11,104,254</u>	<u>\$ 22,323,929</u>	<u>\$ 23,069,367</u>	<u>\$ 32,822,580</u>	<u>\$ 34,173,621</u>

Additional information on the City's capital assets can be found in Note 4 and Note D of the "Notes to the Financial Statements" of this report.

**Long-term debt.** At the end of the 2004 fiscal year, the City of Muskegon Heights had total outstanding debt of \$20,540,767 consisting of general obligations bonds, revenue bonds, capital leases, installment purchase agreements, and accumulated compensated absences. The general obligation debt of \$2,165,000 in governmental funds and \$660,000 in the component unit, Muskegon Heights Downtown Development Authority, are backed by the full-faith and credit of the City. Total outstanding debt has increased due the addition of \$1,500,000 in new general obligation bonds in governmental activities for the City's fiscal stabilization. In 2003, 94% of the City's outstanding debt represented in table below was recorded as revenue bonds, for business activity. In 2004, revenue bonds in business activity represent 87% of the total debt. The payment of the revenue bonds is anticipated through the revenues generated from the water filtration and sewer services in the enterprise funds.

**CITY OF MUSKEGON HEIGHTS OUTSTANDING DEBT**

	Governmental Activities		Business-type Activities		Total	
	2004	2003	2004	2003	2004	2003
General obligation bonds	\$ 2,165,000	\$ 685,000	\$ -	\$ -	\$ 2,165,000	\$ 685,000
Capital leases	68,277	98,306	-	-	68,277	98,306
Installment purchase agreements	95,475	192,399	-	-	95,475	192,399
Note payable	-	-	-	-	-	-
Accumulated compensated absences	397,514	426,305	-	-	397,514	426,305
Revenue bonds	-	-	17,814,501	18,216,799	17,814,501	18,216,799
Total	<u>\$ 2,726,266</u>	<u>\$ 1,402,010</u>	<u>\$ 17,814,501</u>	<u>\$ 18,216,799</u>	<u>\$ 20,540,767</u>	<u>\$ 19,618,809</u>

The net increase in outstanding debt in 2004 was \$921,942. This increase was due to normal debt payoffs as provided for in the fiscal year 2004 Budget, offset by the new \$1,500,000 fiscal stabilization bond.

Additional information on the City of Muskegon Heights' long-term debt can be found in Note I of the notes to the financial statements, beginning on page 26.

### **General Economic Overview**

The City of Muskegon Heights continues to face many of the same economic challenges facing many of the other municipalities in the Western Michigan Region and the state. The city council still maintains that fiscal accountability and financial stability are its top priorities. They remain the greatest challenges facing our community.

The City's General Fund operations are comprised of three major revenue sources: state revenue sharing, local income tax revenue, and property taxes. As has been the case the past few years, state revenue sharing and local income tax revenue are expected to decline in 2005, with property tax revenues growing slightly. Near the end of the 2004 fiscal year, the City obtained fiscal stability bonds, which allowed the city to pay off its lingering operating deficit. In 2005, the challenge will be making the necessary operational adjustments to maintain the positive fund balance, account for new debt service and continue to provide the community with the services it demands.

Planning for the challenges of the future has been aided by the fact the City ended the year with labor negotiations complete and multi-year contracts in place for all of its bargaining units. There will only be one contract open for negotiations in the 2005 fiscal year. The City Council also authorized two additional mills that will be levied for the first time in 2005. In an effort to stabilize costs, the City has continued to freeze any additions to the full-time work force and the City will rely more heavily on part-time workers. We expect this trend to continue given the significant savings realized by using a part-time labor force.

There are a number of external factors that will also have a significant impact on the city and its economic future. In December of 2004, The DANA Corporation, one of the 10 largest employers in the City, indicated they would be closing manufacturing operations in Muskegon in the fall of 2005. Among the facilities being closed is one in the City of Muskegon Heights. The combined property and income taxes of this facility are significant and the City will have to make adjustments to account for the immediate loss in income tax revenue and the gradual loss of property tax revenue. The City of Muskegon Heights has also joined other Muskegon County Wastewater Management System users in reducing the amount of debt for the Sappi Corporation, one of the largest employers in Muskegon County and largest corporate user of the County-wide Wastewater Management System. It is hoped that this reduction in costs will help cement the company's long-term future here in Muskegon County.

The City continues to be optimistic about the long-term projects it is working on and the far reaching impact they can have on the community's economic stability. The Bennett Pump property has now had all of the structures demolished and the City anticipates having it ready for industrial redevelopment by the end of 2005. The former Wastewater Treatment Plant has moved closer to our ultimate goal of redevelopment of the site into single and multi-family housing. The Centennial Plaza site is expected to begin construction before the fall of 2005.

The City of Muskegon Heights like many other governmental entities will be looking more closely at the services it provides and the necessity and costs of providing those services. The City expects to be more involved in providing services jointly with other municipalities, cooperative purchasing and eliminating services duplicated by another organization.

The City's business-type activities have experienced some declines in cash flows and fund balances but overall remain in much better shape than the governmental activities. In the spring of 2005, City Council approved an increase of approximately 9% in the water rate charged to city customers. This rate increase is needed for operations and system improvements. The City Council also increases the sewer commodity rate by 7% and the debt service rate by 25%. These were necessary to account for the operational reductions from closing of the DANA facility mentioned above and the increased cost due to the Sappi Corporation's debt restructuring.

### **Requests for Information**

This financial report is designed to provide a general overview of the City of Muskegon Heights' finances for all those with an interest. Questions concerning any of the information provided in this report or requests for additional information should be addressed to the City of Muskegon Heights, Finance Department, 2724 Peck Street, Muskegon Heights, Michigan 49444, (231) 733-8870.

# BRICKLEY DELONG

CERTIFIED PUBLIC ACCOUNTANTS

## INDEPENDENT AUDITORS' REPORT

June 28, 2005

City Council  
City of Muskegon Heights  
Muskegon Heights, Michigan

We have audited the accompanying financial statements of the governmental activities, the business-type activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of the City of Muskegon Heights as of and for the year ended December 31, 2004, which collectively comprise the City's financial statements as listed in the table of contents. These financial statements are the responsibility of the City of Muskegon Heights' management. Our responsibility is to express opinions on these financial statements based on our audit.

We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards*, issued by the Comptroller General of the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinions.

In our opinion, the financial statements referred to above present fairly, in all material respects, the respective financial position of the governmental activities, the business-type activities, the discretely presented component unit, each major fund, and the aggregate remaining fund information of the City of Muskegon Heights, as of December 31, 2004, and the respective changes in financial position and cash flows, where applicable, thereof for the year then ended in conformity with accounting principles generally accepted in the United States of America.

In accordance with *Government Auditing Standards* we have also issued our report dated June 28, 2005, on our consideration of the City of Muskegon Heights' internal control over financial reporting and on our tests of its compliance with certain provisions of laws, regulations contracts and grants. That report is an integral part of an audit performed in accordance with *Government Auditing Standards* and should be read in conjunction with this report in considering the results of our audit.

The managements' discussion and analysis and budgetary comparison information on pages i through x and 34 through 39, is not a required part of the basic financial statement but are supplemental information required by accounting principles generally accepted in the United States of America. We have applied certain limited procedures, which consisted principally of inquiries of management regarding the methods of measurement and presentation of the supplemental information. However, we did not audit the information and express no opinion on it.

BRICKLEY DELONG

City Council  
June 28, 2005  
Page 2

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise the City of Muskegon Heights' basic financial statements. The combining nonmajor fund financial statements are presented for purposes of additional analysis and are not a required part of the basic financial statements. The combining nonmajor fund financial statements have been subjected to the auditing procedures applied in the audit of the basic financial statements and, in our opinion, are fairly stated in all material respects in relation to the basic financial statements taken as a whole.

*Brickley DeLong, PLC*



City of Muskegon Heights  
STATEMENT OF NET ASSETS  
December 31, 2004

	ASSETS			Component unit
	Governmental activities	Business-type activities	Total	Downtown Development Authority
CURRENT ASSETS				
Cash and investments	\$ 1,053,678	\$ 2,529,388	\$ 3,583,066	\$ 267,744
Receivables	635,390	563,425	1,198,815	117,261
Due from component unit	10,746	-	10,746	-
Due from primary government	-	-	-	4,918
Internal balances	11,512	(11,512)	-	-
Due from other governmental units	546,527	-	546,527	-
Inventories	83,080	24,546	107,626	-
Prepaid items	138,143	-	138,143	-
Total current assets	2,479,076	3,105,847	5,584,923	389,923
NONCURRENT ASSETS				
Restricted assets	-	3,632,044	3,632,044	-
Capital assets, net				
Nondepreciable	254,408	40,012	294,420	294,635
Depreciable	10,244,243	22,283,917	32,528,160	616,598
Bond issue costs, net	50,869	572,981	623,850	-
Special assessments receivable	5,714	-	5,714	-
Notes receivable	-	-	-	26,000
Total noncurrent assets	10,555,234	26,528,954	37,084,188	937,233
Total assets	13,034,310	29,634,801	42,669,111	1,327,156
LIABILITIES AND NET ASSETS (DEFICIT)				
CURRENT LIABILITIES				
Accounts payable and accrued liabilities	325,042	674,781	999,823	20,996
Due to component unit	4,918	-	4,918	-
Due to primary government	-	-	-	10,746
Due to other governmental units	3,288	-	3,288	82,451
Deferred revenue	1,056,777	41,234	1,098,011	163,382
Bonds, capital leases and contracts, due within one year	103,000	420,000	523,000	28,500
Compensated absences due within one year	110,000	-	110,000	-
Accrued interest, due within one year	12,180	147,721	159,901	8,903
Total current liabilities	1,615,205	1,283,736	2,898,941	314,978
NONCURRENT LIABILITIES				
Bonds, capital leases and contracts, less amounts due within one year	2,225,752	17,394,501	19,620,253	789,620
Compensated absences, less amounts due within one year	287,514	-	287,514	-
Total noncurrent liabilities	2,513,266	17,394,501	19,907,767	789,620
Total liabilities	4,128,471	18,678,237	22,806,708	1,104,598
NET ASSETS (DEFICIT)				
Invested in capital assets, net of related debt	9,669,899	6,002,660	15,672,559	93,113
Restricted for:				
Capital projects	25,933	405,084	431,017	-
Highways and streets	184,769	-	184,769	-
Debt service	4,327	1,444,862	1,449,189	-
Non-expendable perpetual care	497,124	-	497,124	-
Unrestricted	(1,476,213)	3,103,958	1,627,745	129,445
Total net assets	\$ 8,905,839	\$ 10,956,564	\$ 19,862,403	\$ 222,558

The accompanying notes are an integral part of this statement.

City of Muskegon Heights  
STATEMENT OF ACTIVITIES  
For the year ended December 31, 2004

Functions/Programs	Net (Expense) Revenue and Changes in Net Assets							
	Expenses	Program Revenue			Primary Government			Component Unit
		Charges for services	Operating grants and contributions	Capital grants and contributions	Governmental activities	Business-type activities	Total	Downtown Development Authority
Primary government								
Governmental activities								
General government	\$ 2,174,833	\$ 228,237	\$ 47,927	\$ -	\$ (1,898,669)	\$ -	\$ (1,898,669)	\$ -
Public safety	3,376,259	245,429	53,478	107,938	(2,969,414)	-	(2,969,414)	-
Public works	2,266,537	351,706	870,732	355,000	(689,099)	-	(689,099)	-
Community and economic development	744,461	13,063	762,839	-	31,441	-	31,441	-
Culture and recreation	314,126	24,260	50,000	-	(239,866)	-	(239,866)	-
Interest on long-term debt	59,984	-	95,616	-	35,632	-	35,632	-
Total governmental activities	8,936,200	862,695	1,880,592	462,938	(5,729,975)	-	(5,729,975)	-
Business-type activities:								
Sewer	792,153	747,955	-	-	-	(44,198)	(44,198)	-
Water	1,225,426	1,306,940	-	-	-	81,514	81,514	-
Water Supply	2,796,131	2,230,689	-	-	-	(565,442)	(565,442)	-
Total business-type activities	4,813,710	4,285,584	-	-	-	(528,126)	(528,126)	-
Total primary government	\$ 13,749,910	\$ 5,148,279	\$ 1,880,592	\$ 462,938	(5,729,975)	(528,126)	(6,258,101)	-
Component unit								
Downtown Development Authority								
Community and economic development	\$ 369,294	\$ 62,334	\$ 2,000	\$ -	-	-	-	(304,960)
General revenues:								
Property taxes					1,961,330	-	1,961,330	353,633
Income taxes					1,020,227	-	1,020,227	-
Franchise fees					91,874	-	91,874	-
Grants and contributions not restricted to specific programs					1,926,545	-	1,926,545	-
Unrestricted investment earnings					39,005	100,550	139,555	3,801
Miscellaneous					137,505	-	137,505	-
Loss on sale of capital asset					(21,423)	-	(21,423)	-
Transfers					24,268	(24,268)	-	-
Total general revenues, special items, and transfers					5,179,331	76,282	5,255,613	357,434
Change in net assets					(550,644)	(451,844)	(1,002,488)	52,474
Net assets at January 1, 2004, restated					9,456,483	11,408,408	20,864,891	170,084
Net assets at December 31, 2004					\$ 8,905,839	\$ 10,956,564	\$ 19,862,403	\$ 222,558

The accompanying notes are an integral part of this statement.

City of Muskegon Heights  
**BALANCE SHEET**  
Governmental Funds  
December 31, 2004

	General Fund	Other governmental funds	Total governmental funds
ASSETS			
Cash and investments	\$ 385,762	\$ 667,916	\$ 1,053,678
Receivables			
Property taxes	286,172	8,752	294,924
Income taxes	128,054	-	128,054
Special assessments	-	5,714	5,714
Other	121,402	54,508	175,910
Due from other funds	350,339	276,640	626,979
Due from component unit	10,746	-	10,746
Due from other governmental units	345,184	201,343	546,527
Inventories	14,080	-	14,080
Prepaid items	138,143	-	138,143
Total assets	<u>\$ 1,779,882</u>	<u>\$ 1,214,873</u>	<u>\$ 2,994,755</u>
LIABILITIES AND FUND BALANCES			
Liabilities			
Accounts payable	\$ 214,194	\$ 56,648	\$ 270,842
Accrued liabilities	43,357	8,568	51,925
Customer deposits	-	2,075	2,075
Due to other funds	123,991	491,476	615,467
Due to component unit	-	4,918	4,918
Due to other governmental units	3,288	-	3,288
Deferred revenue	1,016,156	53,129	1,069,285
Total liabilities	1,400,986	616,814	2,017,800
Fund balances			
Reserved for:			
Inventories	14,080	-	14,080
Prepaid items	138,143	-	138,143
Debt service	-	4,327	4,327
Capital projects	-	25,933	25,933
Perpetual care	-	497,124	497,124
Unreserved			
General Fund	226,673	-	226,673
Special revenue funds	-	70,675	70,675
Total fund balances	378,896	598,059	976,955
Total liabilities and fund balances	<u>\$ 1,779,882</u>	<u>\$ 1,214,873</u>	<u>\$ 2,994,755</u>

The accompanying notes are an integral part of this statement.

City of Muskegon Heights  
**RECONCILIATION OF THE BALANCE SHEET OF GOVERNMENTAL FUNDS  
 TO THE STATEMENT OF NET ASSETS**  
 December 31, 2004

Total fund balance—governmental funds		\$ 976,955
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Amounts reported for governmental activities in the Statement of Net Assets  
are different because:

Inventory of houses recorded on the Statement of Net Assets that are unavailable and are not reported in the governmental funds.		69,000
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Capital assets used in governmental activities are not financial resources and are not reported in the governmental funds.

Cost of capital assets	\$ 23,104,305	
Accumulated depreciation and amortization	<u>(12,605,654)</u>	10,498,651

Bond issuance costs are not capitalized and amortized in the governmental funds

Bond issue costs	51,731	
Accumulated amount	<u>(862)</u>	50,869

Other receivables in governmental activities not reported in the governmental funds.

48,810

Long-term liabilities in governmental activities are not due and payable in the current period and are not reported in the governmental funds.

Long-term liabilities	(2,328,752)	
Compensated absences	<u>(397,514)</u>	(2,726,266)

Accrued interest in governmental activities is not reported in the governmental funds.

(12,180)

Net assets of governmental activities in the Statement of Net Assets		\$ <u><u>8,905,839</u></u>
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The accompanying notes are an integral part of this statement.

City of Muskegon Heights  
**STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES (DEFICITS)**  
Governmental Funds  
For the year ended December 31, 2004

	General Fund	Other governmental funds	Total governmental funds
REVENUES			
Taxes	\$ 2,954,574	\$ 54,335	\$ 3,008,909
Licenses and permits	110,712	-	110,712
Intergovernmental revenues			
Federal	133,873	676,330	810,203
State	1,892,754	942,732	2,835,486
Charges for services	764,917	178,940	943,857
Fines and forfeitures	15,571	-	15,571
Investment earnings	18,600	20,405	39,005
Other	133,255	97,835	231,090
Total revenues	6,024,256	1,970,577	7,994,833
EXPENDITURES			
Current			
General government	1,947,257	178,331	2,125,588
Public safety	3,237,305	-	3,237,305
Public works	728,496	702,210	1,430,706
Community and economic development	13,321	526,261	539,582
Culture and recreation	182,610	107,687	290,297
Debt service			
Principal	26,957	119,996	146,953
Interest and fees	2,540	57,416	59,956
Capital outlay	156,678	57,434	214,112
Total expenditures	6,295,164	1,749,335	8,044,499
Excess of revenues over (under) expenditures	(270,908)	221,242	(49,666)
OTHER FINANCING SOURCES (USES)			
Proceeds from long-term debt, net	1,448,269	-	1,448,269
Proceeds from sale of fixed assets	27,016	-	27,016
Transfers in	40,000	138,805	178,805
Transfers out	(41,018)	(113,519)	(154,537)
Total other financing sources (uses)	1,474,267	25,286	1,499,553
Net change in fund balances (deficit)	1,203,359	246,528	1,449,887
Fund balances (deficit) at January 1, 2004, restated	(824,463)	351,531	(472,932)
Fund balances at December 31, 2004	\$ 378,896	\$ 598,059	\$ 976,955

The accompanying notes are an integral part of this statement.

City of Muskegon Heights  
**RECONCILIATION OF THE STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN  
FUND BALANCES (DEFICITS) OF GOVERNMENTAL FUNDS TO THE STATEMENT OF ACTIVITIES**  
For the year ended December 31, 2004

Net change in fund balances—total governmental funds		\$ 1,449,887
Amounts reported for governmental activities in the Statement of Activities are different because:		
Revenues reported in the Statement of Activities that does not provide current financial resources are not reported as revenue in the governmental funds.		105,701
Net expenditures recorded in the Statement of Activities related to the inventory of houses, but was recorded in the prior year as expenditures in the governmental funds.		(187,142)
Governmental funds report outlays for capital assets as expenditures; in the Statement of Activities, these costs are depreciated and amortized over their estimated useful lives.		
Depreciation and amortization expense	\$ (1,069,838)	
Capital outlay	<u>461,739</u>	(608,099)
Proceeds from bond issuance is an other financing source in the governmental funds, but the proceeds increase long-term debt in the Statement of Net Assets.		(1,500,000)
Bond premiums are amortized over time in the Statement of Activities, but are recorded in full in the year paid in the governmental funds		50,869
Governmental funds report the entire proceeds from the sale of fixed assets as revenue in the governmental funds. In contrast, the Statement of Activities reports only the gain or loss on sale of capital assets		(38,438)
Repayment of principal on long-term debt is an expenditure in the governmental funds, but the repayment reduces long-term liabilities in the Statement of Net Assets.		146,953
Accrued interest on long-term debt is recorded in the Statement of Activities when incurred, but is not reported in the governmental funds until paid.		834
Increases in the compensated absences are reported as expenses when earned in the Statement of Activities and reported as expenditures when financial resources are used in the governmental funds.		<u>28,791</u>
Change in net assets of governmental activities		<u><u>\$ (550,644)</u></u>

The accompanying notes are an integral part of this statement.

City of Muskegon Heights  
STATEMENT OF NET ASSETS  
Enterprise Funds  
December 31, 2004

ASSETS

	Sewer	Water	Water Supply	Total
CURRENT ASSETS				
Cash and investments	\$ 1,233,474	\$ 240,218	\$ 1,055,696	\$ 2,529,388
Accounts receivable	210,649	352,776	-	563,425
Due from other funds	81,072	-	678,339	759,411
Inventories	-	17,050	7,496	24,546
Total current assets	1,525,195	610,044	1,741,531	3,876,770
NONCURRENT ASSETS				
Restricted assets	-	-	3,632,044	3,632,044
Capital assets				
Land	2,246	-	37,766	40,012
Buildings and system	-	21,920	89,306	111,226
Plants and infrastructure	3,172,580	1,911,658	24,751,248	29,835,486
Machinery and equipment	259,736	233,050	351,449	844,235
Less accumulated depreciation	(1,988,203)	(1,631,467)	(4,887,360)	(8,507,030)
Net capital assets	1,446,359	535,161	20,342,409	22,323,929
Bond issuance costs, net	-	-	572,981	572,981
Total noncurrent assets	1,446,359	535,161	24,547,434	26,528,954
Total assets	2,971,554	1,145,205	26,288,965	30,405,724

LIABILITIES AND NET ASSETS (DEFICIT)

CURRENT LIABILITIES				
Accounts payable	67,535	5,857	548,161	621,553
Accrued liabilities	15,225	14,884	170,840	200,949
Due to other funds	1,134	767,755	2,034	770,923
Deferred revenue	-	41,234	-	41,234
Bonds, capital leases and contracts, due within one year	100,000	-	320,000	420,000
Total current liabilities	183,894	829,730	1,041,035	2,054,659
NONCURRENT LIABILITIES				
Bonds, capital leases and contracts, less amounts due within one year	344,501	-	17,050,000	17,394,501
Total liabilities	528,395	829,730	18,091,035	19,449,160
NET ASSETS (DEFICIT)				
Invested in capital assets, net of related debt	1,001,858	535,161	4,465,641	6,002,660
Restricted for:				
Capital projects	-	-	405,084	405,084
Debt service	-	-	1,444,862	1,444,862
Unrestricted	1,441,301	(219,686)	1,882,343	3,103,958
Total net assets	\$ 2,443,159	\$ 315,475	\$ 8,197,930	\$ 10,956,564

The accompanying notes are an integral part of this statement.

City of Muskegon Heights  
**STATEMENT OF REVENUES, EXPENSES AND CHANGES IN NET ASSETS**  
Enterprise Funds  
For the year ended December 31, 2004

	Sewer	Water	Water Supply	Total
REVENUES				
Charges for services	\$ 747,955	\$ 1,306,940	\$ 2,230,689	\$ 4,285,584
OPERATING EXPENSES				
Administration	80,000	120,417	80,000	280,417
Operations	580,347	1,051,428	1,007,066	2,638,841
Depreciation and amortization	56,585	53,581	705,198	815,364
Total operating expenses	716,932	1,225,426	1,792,264	3,734,622
Operating income	31,023	81,514	438,425	550,962
NONOPERATING REVENUES (EXPENSES)				
Investment earnings	13,898	4,806	81,846	100,550
Interest expense	(75,221)	-	(1,003,867)	(1,079,088)
Total nonoperating revenue (expenses)	(61,323)	4,806	(922,021)	(978,538)
Income (loss) before transfers	(30,300)	86,320	(483,596)	(427,576)
Transfers out	-	-	(24,268)	(24,268)
Change in net assets	(30,300)	86,320	(507,864)	(451,844)
Total net assets at January 1, 2004	2,473,459	229,155	8,705,794	11,408,408
Total net assets at December 31, 2004	\$ 2,443,159	\$ 315,475	\$ 8,197,930	\$ 10,956,564

The accompanying notes are an integral part of this statement.



City of Muskegon Heights  
**STATEMENT OF CASH FLOWS**  
Enterprise Funds  
For the year ended December 31, 2004

	Sewer	Water	Water Supply	Total
<b>CASH FLOWS FROM OPERATING ACTIVITIES</b>				
Receipts from customers	\$ 758,329	\$ 1,235,674	\$ 1,530,418	\$ 3,524,421
Receipts from interfund services provided	3,497	10,674	1,336,881	1,351,052
Payments to suppliers	(484,259)	(193,914)	(728,946)	(1,407,119)
Payments to employees	(100,492)	(169,857)	(329,380)	(599,729)
Payments for interfund services	<u>(68,358)</u>	<u>(1,172,532)</u>	<u>(403,678)</u>	<u>(1,644,568)</u>
Net cash provided by (used for) operating activities	108,717	(289,955)	1,405,295	1,224,057
<b>CASH FLOWS FROM NONCAPITAL FINANCING ACTIVITIES</b>				
Operating subsidies and transfers to other funds	<u>-</u>	<u>-</u>	<u>(24,268)</u>	<u>(24,268)</u>
<b>CASH FLOWS FROM CAPITAL AND RELATED FINANCING ACTIVITIES</b>				
Purchases of capital assets	-	-	(69,926)	(69,926)
Principal and interest paid on capital debt	<u>(173,111)</u>	<u>-</u>	<u>(1,282,494)</u>	<u>(1,455,605)</u>
Net cash used for capital and related financing activities	(173,111)	-	(1,352,420)	(1,525,531)
<b>CASH FLOW FROM INVESTING ACTIVITIES</b>				
Advances to other funds	290,000	-	-	290,000
Investment earnings	<u>13,898</u>	<u>4,806</u>	<u>81,846</u>	<u>100,550</u>
Net cash provided by investing activities	303,898	4,806	81,846	390,550
Net increase (decrease) in cash and investments	239,504	(285,149)	110,453	64,808
Cash and investments at January 1, 2004	<u>993,970</u>	<u>525,367</u>	<u>4,577,287</u>	<u>6,096,624</u>
Cash and investments at December 31, 2004	<u>\$ 1,233,474</u>	<u>\$ 240,218</u>	<u>\$ 4,687,740</u>	<u>\$ 6,161,432</u>
<b>Reconciliation of cash and investments to the balance sheet</b>				
Cash and investments	\$ 1,233,474	\$ 240,218	\$ 1,055,696	\$ 2,529,388
Restricted assets	<u>-</u>	<u>-</u>	<u>3,632,044</u>	<u>3,632,044</u>
	<u>\$ 1,233,474</u>	<u>\$ 240,218</u>	<u>\$ 4,687,740</u>	<u>\$ 6,161,432</u>
<b>Reconciliation of operating income to net cash provided by (used for) operating activities</b>				
Operating income	\$ 31,023	\$ 81,514	\$ 438,425	\$ 550,962
Adjustments to reconcile operating income to net cash provided by (used for) operating activities				
Depreciation and amortization expense	56,585	53,581	705,198	815,364
Change in assets and liabilities				
Receivables, net	13,871	(67,005)	37,338	(15,796)
Internal activity	11,642	(348,509)	278,095	(58,772)
Inventories	-	(4,220)	1,552	(2,668)
Accounts and other payables	(7,344)	(8,650)	(40,112)	(56,106)
Accrued liabilities	<u>2,940</u>	<u>3,334</u>	<u>(15,201)</u>	<u>(8,927)</u>
Net cash provided by (used for) operating activities	<u>\$ 108,717</u>	<u>\$ (289,955)</u>	<u>\$ 1,405,295</u>	<u>\$ 1,224,057</u>

The accompanying notes are an integral part of this statement.

City of Muskegon Heights  
**STATEMENT OF FIDUCIARY NET ASSETS**  
December 31, 2004

	Employee Benefit Plan	Private Purpose Trust Fund - Simple	Agency Funds
<b>ASSETS</b>			
Cash and investments	\$ 802,880	\$ 3,215	\$ 631,974
Accounts receivable	<u>-</u>	<u>-</u>	<u>102,712</u>
Total assets	802,880	3,215	734,686
<b>LIABILITIES</b>			
Accounts payable	-	-	103,411
Due to other governmental units	-	-	597,653
Deposits held for others	<u>-</u>	<u>-</u>	<u>33,622</u>
Total liabilities	<u>-</u>	<u>-</u>	<u>734,686</u>
<b>NET ASSETS</b>			
Held in trust for benefits and other purposes	<u>\$ 802,880</u>	<u>\$ 3,215</u>	<u>\$ -</u>

The accompanying notes are an integral part of this statement.

City of Muskegon Heights  
**STATEMENT OF CHANGES IN FIDUCIARY NET ASSETS**  
For the year ended December 31, 2004

	Employee Benefit Plan	Private Purpose Trust Fund - Simple
<b>ADDITIONS</b>		
Employee contributions	\$ 16,316	\$ -
Investment gain	<u>42,834</u>	<u>-</u>
	59,150	-
<b>DEDUCTIONS</b>		
Benefits	35,865	-
Fees	<u>-</u>	<u>44</u>
	<u>35,865</u>	<u>44</u>
Change in net assets	23,285	(44)
Net assets at January 1, 2004	<u>779,595</u>	<u>3,259</u>
Net assets at December 31, 2004	<u><u>\$ 802,880</u></u>	<u><u>\$ 3,215</u></u>

The accompanying notes are an integral part of this statement.

City of Muskegon Heights  
**NOTES TO FINANCIAL STATEMENTS**  
December 31, 2004

**NOTE A—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**

The financial statements of the City of Muskegon Heights (City) have been prepared in conformity with accounting principles generally accepted in the United States of America (GAAP) as applied to government units. The Governmental Accounting Standards Board (GASB) is the accepted standard-setting body for establishing governmental accounting and financial reporting principles. The more significant of the City's accounting policies are described below.

Effective January 1, 2003, the City and Downtown Development Authority adopted GASB Statement No. 34, *Basic Financial Statements – and Management's Discussion and Analysis – for State and Local Governments*, as amended by GASB Statement No. 37 and No. 38. These statements primarily establish standards for external financial reporting for state and local governments. Certain significant changes in these statements include the following:

- A Management Discussion and Analysis (MD&A) section providing an analysis of the City's overall financial position and results of operations.
- Government-wide financial statements prepared using full accrual accounting for all of the City's activities.
- A change in the fund financial statements to focus on the major funds.
- Expansion of footnote disclosures.
- These and other changes are reflected in the accompanying financial statements, including notes to financial statements.

**1. Report Entity**

The City of Muskegon Heights' (City) is a municipal corporation governed by an elected mayor and six-member council. The accompanying financial statements present the government and its component units, entities for which the government is considered to be financially accountable. Each discretely presented component unit is reported in a separate column in the government-wide financial statements (see note below for description) to emphasize that it is legally separate from the government.

***Discretely presented component unit***

The discretely presented component unit is reported in a separate column in the combined financial statements to emphasize that it is legally separate from the primary government. The discretely presented component unit has a December 31 fiscal year end. The discretely presented component unit is the Downtown Development Authority (DDA).

The DDA board is appointed by the City Council, but the Authority operates as a separate entity. The DDA board can authorize and issue debt independent from the City. The DDA is presented as a governmental fund type.

City of Muskegon Heights  
**NOTES TO THE FINANCIAL STATEMENTS—CONTINUED**  
December 31, 2004

**NOTE A—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—Continued**

**2. Government-Wide and Fund Financial Statements**

The government-wide financial statements (i.e., the statement of net assets and the statement of changes in net assets) report information on all of the nonfiduciary activities of the primary government and its component units. For the most part, the effect of interfund activity has been removed from these statements.

Governmental activities, which normally are supported by taxes and intergovernmental revenues, are reported separately from business-type activities, which rely to a significant extent on fees and charges for support. Likewise, the primary government is reported separately from certain legally separate component units for which the primary government is financially accountable.

The statement of activities demonstrates the degree to which the direct expenses of a given function or segment are offset by program revenues. Direct expenses are those that are clearly identifiable with a specific function or segment. Program revenues include 1) charges to customers or applicants who purchase, use, or directly benefit from goods, services, or privileges provided by a given function or segment and 2) grants and contributions that are restricted to meeting the operational or capital requirement of a particular function or segment. Taxes and other items not properly included among program revenues are reported instead as general revenues.

Separate financial statements are provided for governmental funds, proprietary funds, and fiduciary funds, even though the latter are excluded from the government-wide financial statements. Major individual governmental funds and major individual enterprise funds are reported as separate columns in the fund financial statements.

**3. Measurement Focus, Basis of Accounting and Financial Statement Presentation**

The government-wide financial statements are reported using the economic resources measurement focus and the accrual basis of accounting, as are the proprietary fund and fiduciary fund financial statements. Revenues are recorded when earned and expenses are recorded when a liability is incurred, regardless of the timing of related cash flows. Property taxes are recognized as revenues in the year for which they are levied. Grants and similar items are recognized as revenue as soon as all eligibility requirements imposed by the provider have been met.

Governmental fund financial statements are reported using the current financial resources measurement focus and the modified accrual basis of accounting. Revenues are recognized as soon as they are both measurable and available. Revenues are considered to be available when they are collectible within the current period or soon enough thereafter to pay liabilities of the current period. For this purpose, the government considers revenues to be available if they are collected within 60 days of the end of the current fiscal period. Expenditures generally are recorded when a liability is incurred, as under accrual accounting. However, debt service expenditures, as well as expenditures related to compensated absences and claims and judgments, are recorded only when payment is due.

Property taxes, income taxes, franchise taxes, licenses and interest associated with the current fiscal period are all considered to be susceptible to accrual and so have been recognized as revenues of the current fiscal period. Only the portion of special assessments receivable due within the current fiscal period is considered to be susceptible to accrual as revenue of the current period. All other revenue items are considered to be measurable and available only when cash is received by the government.

City of Muskegon Heights  
**NOTES TO THE FINANCIAL STATEMENTS—CONTINUED**  
December 31, 2004

**NOTE A—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—Continued**

**3. Measurement Focus, Basis of Accounting and Financial Statement Presentation—Continued**

The City reports the following major governmental funds:

The General Fund is the government's primary operating fund. It accounts for all financial resources of the general government, except those required to be accounted for in another fund.

The City reports the following three major proprietary funds:

The Sewer Fund operates the City's sewage pumping station, collection systems and pays for access to the county's sewage treatment plant.

The Water Fund operates the City's water distribution system.

The Water Supply Fund operates the City's water treatment plant. The plant provides water to the City and two adjacent municipalities.

Additionally, the City reports the following fund types:

The Pension Trust Fund accounts for the activities of the City's employees retirement plan, which accumulates resources for pension benefit payments.

The Private Purpose Trust Fund is a fund comprised of employee contributions for the purpose of purchasing cards and flowers as sympathy for illness and death.

Private-sector standards of accounting and financial reporting issued prior to December 1, 1989, generally are followed in both the government-wide and proprietary fund financial statements to the extent that those standards do not conflict with or contradict guidance of the Government Accounting Standards Board. Governments also have the option of following subsequent private-sector guidance for their business-type activities and enterprise funds, subject to this same limitation. The City has elected not to follow subsequent private-sector guidance.

As a general rule the effect of interfund activity has been eliminated from the government-wide financial statements. Exceptions to this general rule are payments-in-lieu of taxes and other charges between the City's water and sewer function and various other functions of the government. Elimination of these charges would distort the direct costs and program revenues reported for the various functions concerned.

Amounts reported as program revenues include 1) charges to customers or applicants for goods, services or privileges provided, 2) operating grants and contributions and 3) capital grants and contributions, including special assessments. Internally dedicated resources are reported as general revenues rather than as program revenues. Likewise, general revenues include all taxes.

Proprietary funds distinguish operating revenues and expenses from nonoperating items. Operating revenues and expenses generally result from providing services and producing and delivering goods in connection with a proprietary fund's principal ongoing operations. The principal operating revenues are charges to customers for sales and services. The enterprise funds also recognize as operating revenue the portion of tap fees intended to recover the cost of connecting new customers to the system. Operating expenses for enterprise funds include the cost of sales and services, administrative expenses and depreciation on capital assets. All revenues and expenses not meeting this definition are reported as nonoperating revenues and expenses.

When both restricted and unrestricted resources are available for use, it is the City's policy to use restricted resources first, then unrestricted resources as they are needed.

City of Muskegon Heights  
**NOTES TO THE FINANCIAL STATEMENTS—CONTINUED**  
December 31, 2004

**NOTE A—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—Continued**

**4. Assets, Liabilities and Net Assets or Equity**

**a. Deposits and Investments**

The City's cash and cash equivalents are considered to be cash on hand, demand deposits and short-term investments with original maturities of three months or less from the date of acquisition.

The City has adopted an investment policy in compliance with State of Michigan statutes. Those statutes authorize the City to invest in obligations of the United States, certificates of deposit, prime commercial paper, securities guaranteed by United States agencies or instrumentalities, United States government or federal agency obligation repurchase agreements, bankers acceptances, state-approved investment pools and certain mutual funds.

The component unit's cash and investments are maintained within the City's investment pool. All investments are stated at cost or amortized cost.

**b. Receivables and Payables**

Activity between funds that are representative of lending/borrowing arrangements outstanding at the end of the fiscal year are referred to as either "due to/from other funds" (i.e., the current portion of interfund loans) or "advances to/from other funds" (i.e., the non-current portion of interfund loans). All other outstanding balances between funds are reported as "due to/from other funds". Any residual balances outstanding between the governmental activities and business-type activities are reported in the government-wide financial statements as "internal balances".

Advances between funds, as reported in the fund financial statements, are offset by a fund balance reserve account in applicable governmental funds to indicate that they are not available for appropriation and are not expendable available financial resources.

All trade and property tax receivables are shown net of allowance for uncollectibles.

The City bills and collects its own property taxes and also collects taxes for the county, school and State of Michigan. Taxes are levied on each July 1 on the taxable valuation of property (as defined by state statutes) located in the Local Governmental Unit as of the preceding December 31. Uncollectible real property taxes as of the following February 15 are turned over by the City to the County for collection. The County advances the City all these delinquent real property taxes. The delinquent personal property taxes remain the responsibility of the City.

Although the Local Governmental Unit 2004 ad valorem tax is levied and collectible on July 1, 2004, it is the Local Governmental Unit's policy to recognize one half of the current tax levy, if available, in the current year since the millage was approved to finance the City from July 1 through the following June 30. "Available" means collected within the current period or expected to be collected soon enough thereafter to be used to pay liabilities of the current period (60 days).

The 2004 state taxable value for real/personal property of the City totaled approximately \$120,300,000 of which approximately \$8,450,000 was captured by the DDA. The ad valorem taxes levied consisted of 10 mills for operation, 3 mills for sanitation, 3 mills for police, and .35 mills for street lighting for the City's General Fund operating purposes and .5 mills for the Recreation Fund activities. These amounts are recognized in the respective General Fund, Recreation Fund and DDA.

City of Muskegon Heights  
**NOTES TO THE FINANCIAL STATEMENTS—CONTINUED**  
December 31, 2004

**NOTE A—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—Continued**

**4. Assets, Liabilities and Net Assets or Equity—Continued**

**c. Inventories and Prepaid Items**

All inventories are valued at cost using the first-in/first-out(FIFO) method. Inventories of governmental funds are recorded as expenditures when consumed rather than when purchased.

Certain payments to vendors reflect costs applicable to future accounting periods and are recorded as prepaid items in both government-wide and fund financial statements.

**d. Restricted Assets**

Certain proceeds of the Enterprise Fund revenue bonds, as well as certain resources set aside for their repayment, are classified as restricted assets on the balance sheet because they are maintained in separate bank accounts and their use is limited by applicable bond covenants.

**e. Capital Assets**

Capital assets, which include property, plant, equipment and infrastructure assets (e.g., roads, bridges, sidewalks and similar items), are reported in the applicable governmental or business-type activities columns in the government-wide financial statements. Capital assets, other than infrastructure assets, are defined by the government as assets with an initial, individual cost of more than \$5,000 (amount not rounded) and an estimated useful life in excess of two years. The government reports infrastructure assets on a network and subsystem basis. Accordingly, the amounts spent for the construction or acquisition of infrastructure assets are capitalized and reported in the government-wide financial statements regardless of their amount.

In the case of the initial capitalization of general infrastructure assets (i.e., those reported by governmental activities) the government chose to include all such items regardless of their acquisition date or amount. The government was able to estimate the historical cost for the initial reporting of these assets through backtrending (i.e., estimating the current replacement cost of the infrastructure to be capitalized and using an appropriate price-level index to deflate the cost to the acquisition year or estimated acquisition year). As the government constructs or acquires additional capital assets each period, including infrastructure assets, they are capitalized and reported at historical cost. The reported value excludes normal maintenance and repairs which are essentially amounts spent in relation to capital assets that do not increase the capacity or efficiency of the item or extend its useful life beyond the original estimate. In the case of donations the government values these capital assets at the estimated fair value of the item at the date of its donation.

Interest incurred during the construction phase of capital assets of business-type activities is included as part of the capitalized value of the assets constructed.

Property, plant and equipment of the primary government, as well as the component units, is depreciated using the straight-line method over the following estimated useful lives:

<u>Assets</u>	<u>Years</u>
Buildings and access rights	25-50
Public domain infrastructure	20-30
System infrastructure and improvements	10-100
Vehicles and equipment	5-25
Office equipment	5



City of Muskegon Heights  
**NOTES TO THE FINANCIAL STATEMENTS—CONTINUED**  
December 31, 2004

**NOTE A—SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES—Continued**

**4. Assets, Liabilities and Net Assets or Equity—Continued**

**f. Compensated Absences**

City employees are granted vacation and sick leave in varying amounts based on length of service. Accumulated vacation leave must be taken no later than the year after it is earned. Upon termination, employees are paid for unused vacation at their current rates. Sick leave is accumulated at the rate of one day per month of employment. Unused sick leave is accumulated up to 120 days for employees. Unused accumulated sick leave is paid to employees who resign or retire, limited to 50 percent of days accumulated. All vacation and sick pay is accrued when incurred in the government-wide, proprietary and fiduciary fund financial statements. A liability for these amounts is reported in governmental funds only if they have matured, for example, as a result of employee resignations and retirements.

**g. Long-Term Obligations**

In the government-wide financial statements and proprietary fund types in the fund financial statements, long-term debt and other long-term obligations are reported as liabilities in the applicable governmental activities, business-type activities or proprietary fund type statement of net assets. Bond premiums and discounts as well as issuance costs, are deferred and amortized over the life of the bonds using the effective interest method. Bonds payable are reported net of the applicable bond premium or discount. Bond issuance costs are reported as deferred charges and amortized over the term of the related debt.

In the fund financial statements, governmental fund types recognize bond premiums and discounts, as well as bond issuance costs, during the current period. The face amount of debt issued is reported as other financing sources. Premiums received on debt issuances are reported as other financing sources while discounts on debt issuances are reported as other financing uses. Issuance costs, whether or not withheld from the actual debt proceeds received, are reported as debt service expenditures.

**h. Fund Equity**

In the fund financial statements, governmental funds report reservations of fund balance for amounts that are not available for appropriation or are legally restricted by outside parties for use for a specific purpose. Designations of fund balance represent tentative management plans that are subject to change.

**i. Use of Estimates**

The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect certain reported amounts and disclosures.

**NOTE B—STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY**

**1. Budgetary Information**

Annual budgets are adopted on a basis consistent with generally accepted accounting principles for all governmental funds except the capital projects funds, which adopt project-length budgets, and the permanent fund, which is not budgeted. All annual appropriations lapse at fiscal year end.

City of Muskegon Heights  
**NOTES TO THE FINANCIAL STATEMENTS—CONTINUED**  
December 31, 2004

**NOTE B—STEWARDSHIP, COMPLIANCE AND ACCOUNTABILITY—Continued**

**1. Budgetary Information—Continued**

The City follows these procedures in establishing the budgetary information provided in the financial statements:

- a. Prior to the first Monday of November, the City Manager submits to the City Council a proposed operating budget for the fiscal year commencing the following January 1. The operating budget includes proposed expenditures and the means of financing them.
- b. Public hearings are conducted at the City Hall to obtain taxpayer comments.
- c. Not later than the second Monday in December, the budget is legally enacted through passage of a resolution.
- d. Supplemental appropriations, when required to provide for additional expenditures, are matched by additional anticipated revenues or an appropriation of available fund balance and must be approved by the City Council. All appropriations lapse at year end.

The appropriated budget is prepared by fund, function and department. The City's department heads may make transfers of appropriations within a department. Transfers of appropriations between departments require the approval of the City Council. The legal level of budgetary control is the department level. The City Council made several supplemental budgetary appropriations throughout the year.

**2. Excess of Expenditures Over Appropriations**

For the year ended December 31, 2004, expenditures exceeded appropriations in the following funds and departments.

	<u>Amended budget</u>	<u>Actual</u>	<u>Excess</u>
General Fund			
Assessor	\$ 123,788	\$ 126,623	\$ 2,835
Motor pool	70,000	74,267	4,267
Fire	974,099	988,582	14,483
Public works	52,100	55,835	3,735
Traffic Department	12,900	22,025	9,125
Debt Service	16,280	29,497	13,217
Capital outlay	126,500	156,678	30,178
Transfers out	-	41,018	41,018
Major Street Fund			
Winter maintenance	124,000	137,426	13,426
Debt Service	-	18,691	18,691
Local Streets Fund			
Winter maintenance	56,500	78,734	22,234
Recreation Fund	98,000	107,686	9,686

**3. Fund Deficit**

As of December 31, 2004, the City's Major Street Fund, Cemetery Fund and Water Fund had undesignated fund deficits of \$150,402, \$14,987, and \$219,686, respectively. The deficits will be eliminated through future operations, which may include new revenue sources, reduction of operating expenses and interfund transfers.

City of Muskegon Heights  
**NOTES TO THE FINANCIAL STATEMENTS—CONTINUED**  
December 31, 2004

**NOTE C—DEPOSITS AND INVESTMENTS**

**1. Deposits**

The City's deposits are categorized to give an indication of the level of risk assumed by the entity at year end. Category 1 includes deposits insured or collateralized with securities held by the entity or its agent in the entity's name. Category 2 includes deposits collateralized with securities held by the pledging financial institutions' trust department or agent in the entity's name. Category 3 includes deposits which are uncollateralized.

As of December 31, 2004, the City's and component units' carrying amount of deposits was \$1,058,086 and the bank balance was \$1,132,553. Of the bank balance, \$200,808 was covered by federal depository insurance.

**2. Investments**

As of December 31, 2004, the City's investments represented holdings in investment pools, mutual funds, corporate bonds, certificates of deposit, federal agency bonds and mortgage-backed securities. During the year ended December 31, 2004, the City's investments were only in this type of investment. As of December 31, 2004, the Downtown Development Authority investments represented holdings in corporate bonds. During the year ended December 31, 2004, the Downtown Development Authority's investments were only in this type of investment.

The City's investments are categorized below to give an indication of the level of risk assumed by the entity at year end. Category 1 includes investments that are insured or registered, or the securities held by the City or its agent in the City's name. Category 2 includes uninsured and unregistered investments for which the securities are held by the counterparty's trust department or agent in the City's name. Category 3 includes uninsured and unregistered investments for which the securities are held by the counterparty, or by its trust department or agent but not in the City's name. The state-approved investment pools are not categorized as they are synonymous with mutual funds. As of December 31, 2004, the City's fair value in those pools and mutual funds were \$5,890,927.

	Category			Fair value amount
	<u>1</u>	<u>2</u>	<u>3</u>	
Corporate bonds	\$ -	\$ -	\$ 10,994	\$ 10,994
Certificates of Deposit	-	670,185	-	670,185
Federal agency bonds	-	-	165,573	165,573
Mortgage backed securities	-	-	<u>1,125,127</u>	<u>1,125,127</u>
	<u>\$ -</u>	<u>\$ 670,185</u>	<u>\$ 1,301,694</u>	<u>\$ 1,971,879</u>

The composition of pension trust fund investments at fair value is included in the previous paragraph and shown in the following table:

Managed Domestic stock funds	\$ 508,068
Managed Bonds funds	<u>294,812</u>
	<u>\$ 802,880</u>

City of Muskegon Heights  
**NOTES TO THE FINANCIAL STATEMENTS—CONTINUED**  
December 31, 2004

**NOTE C—DEPOSITS AND INVESTMENTS—Continued**

**2. Investments—Continued**

Below is a summary of the combined balance sheet deposits and investments:

	Government activities	Business- type activities	Fiduciary Fund	Total primary government	Component unit
Cash and investments	\$ 1,053,678	\$ 2,529,388	\$ 1,438,069	\$ 5,021,135	\$ 267,744
Restricted assets	<u>-</u>	<u>3,632,014</u>	<u>-</u>	<u>3,632,014</u>	<u>-</u>
Total deposits and investments	<u>\$ 1,053,678</u>	<u>\$ 6,161,402</u>	<u>\$ 1,438,069</u>	<u>\$ 8,653,149</u>	<u>\$ 267,744</u>

**3. Restricted Assets**

Restrictions are placed on assets by bond ordinance and City Council action. At December 31, 2004, restricted cash and investments in the Enterprise funds are restricted as follows:

Water Supply Fund	
Rate Stabilization	\$ 288,866
Repairs and Replacement	405,084
Bond Reserve Fund	1,444,862
Construction	<u>1,493,232</u>
	<u>\$ 3,632,044</u>

**NOTE D—CAPITAL ASSETS**

Capital asset activity for the year ended December 31, 2004 was as follows:

	Balance January 1, 2004	Additions	Deductions	Balance December 31, 2004
<b>Governmental activities:</b>				
<b>Capital assets, not being depreciated:</b>				
Land	\$ 247,908	\$ 16,500	\$ 10,000	\$ 254,408
<b>Capital assets, being depreciated:</b>				
Buildings and improvements	1,235,756	-	-	1,235,756
Infrastructure	18,198,936	-	-	18,198,936
Furniture and equipment	924,923	436,739	35,000	1,326,662
Vehicles	<u>2,148,184</u>	<u>18,500</u>	<u>78,141</u>	<u>2,088,543</u>
Total capital assets being depreciated	22,507,799	455,239	113,141	22,849,897

City of Muskegon Heights  
**NOTES TO THE FINANCIAL STATEMENTS—CONTINUED**  
December 31, 2004

**NOTE D—CAPITAL ASSETS—Continued**

	Balance January 1, <u>2004</u>	<u>Additions</u>	<u>Deductions</u>	Balance December 31, <u>2004</u>
<b>Governmental activities:—Continued</b>				
<b>Less accumulated depreciation for:</b>				
Buildings and improvements	\$ 517,387	\$ 25,704	\$ -	\$ 543,091
Infrastructure	9,653,655	893,196	-	10,546,851
Furniture and equipment	411,874	49,227	16,139	444,962
Vehicles	<u>1,027,603</u>	<u>101,712</u>	<u>58,565</u>	<u>1,070,750</u>
Total accumulated depreciation	<u>11,610,519</u>	<u>1,069,839</u>	<u>74,704</u>	<u>12,605,654</u>
Total capital assets, being depreciated, net	<u>10,897,280</u>	<u>(614,600)</u>	<u>38,437</u>	<u>10,244,243</u>
Capital assets, net	<u>\$11,145,188</u>	<u>\$ (598,100)</u>	<u>\$ 48,437</u>	<u>\$10,498,651</u>
<b>Business-type activities:</b>				
<b>Capital assets, not being depreciated:</b>				
Land	\$ 40,012	\$ -	\$ -	\$ 40,012
<b>Capital assets, being depreciated:</b>				
Buildings and improvements	111,226	-	-	111,226
Plants and infrastructure	29,765,561	69,926	-	29,835,487
Machinery and equipment	<u>844,234</u>	<u>-</u>	<u>-</u>	<u>844,234</u>
Total capital assets, being depreciated	30,721,021	69,926	-	30,790,947
<b>Less accumulated depreciation for:</b>				
Buildings and improvements	111,226	-	-	111,226
Plants and infrastructure	6,787,310	793,007	-	7,580,317
Machinery and equipment	<u>793,130</u>	<u>22,357</u>	<u>-</u>	<u>815,487</u>
Total accumulated depreciated	<u>7,691,666</u>	<u>815,364</u>	<u>-</u>	<u>8,507,030</u>
Total capital assets, being depreciated, net	<u>23,029,355</u>	<u>(745,438)</u>	<u>-</u>	<u>22,283,917</u>
Capital assets, net	<u>\$23,069,367</u>	<u>\$ (745,438)</u>	<u>\$ -</u>	<u>\$22,323,929</u>

Depreciation expense was charged to functions as follows:

<b>Government activities:</b>	
General government	\$ 21,736
Public safety	79,708
Public works	948,768
Culture and recreation	<u>19,627</u>
Total depreciation expense - governmental activities	<u>\$ 1,069,839</u>
<b>Business-type activities:</b>	
Sewer	\$ 56,585
Water	53,581
Water Supply	<u>705,198</u>
Total depreciation expense - business-type activities	<u>\$ 815,364</u>

City of Muskegon Heights  
**NOTES TO THE FINANCIAL STATEMENTS—CONTINUED**  
December 31, 2004

**NOTE D—CAPITAL ASSETS—Continued**

*Discretely presented component units*

Activity for the City for the year ended December 31, 2004 was as follows:

	Balance January 1, 2004	Additions	Deductions	Balance December 31, 2004
Capital assets, not being depreciated:				
Land	\$ 294,635	\$ -	\$ -	\$ 294,635
Capital assets, being depreciated:				
Buildings	753,835	-	-	753,835
Less accumulated depreciation for:				
Buildings	120,111	17,126	-	137,237
Total capital assets, being depreciated, net	<u>633,724</u>	<u>(17,126)</u>	<u>-</u>	<u>616,598</u>
City capital assets, net	\$ <u>928,359</u>	\$ <u>(17,126)</u>	\$ <u>-</u>	\$ <u>911,233</u>

**NOTE E—BOND ISSUANCE COSTS**

	Balance January 1, 2004	Additions	Deletions	Balance December 31, 2004
Water Supply				
Issuance	\$ 383,175	\$ -	\$ -	\$ 383,175
Discount	333,050	-	-	333,050
Sewer				
Discount	<u>9,350</u>	<u>-</u>	<u>-</u>	<u>9,350</u>
Total Bond Issuance Cost	725,575	-	-	725,575
<b>Less Amortization</b>				
Water Supply Fund over 15 years	119,370	23,874	-	143,244
Sewer Fund over 6.5 years	<u>5,754</u>	<u>3,596</u>	<u>-</u>	<u>9,350</u>
	<u>125,124</u>	<u>27,470</u>	<u>-</u>	<u>152,594</u>
Total Bond Issuance cost, Net of Amortization	\$ <u>600,451</u>	\$ <u>(27,470)</u>	\$ <u>-</u>	\$ <u>572,981</u>

**Amortization**

Amortization expense has been charged to interest expense and included in the following functions:

Water Supply	\$ 23,874
Sewer	<u>3,596</u>
	\$ <u>27,470</u>

City of Muskegon Heights  
**NOTES TO THE FINANCIAL STATEMENTS—CONTINUED**  
December 31, 2004

**NOTE F—DEFERRED REVENUE**

Governmental funds report deferred revenue in connection with receivables for revenues that are not considered to be available to liquidate liabilities of the current period. Governmental funds also defer revenue recognition in connection with resources that have been received, but not yet earned. At the end of the current fiscal year, the various components of deferred revenue and unearned revenue reported in the governmental funds were as follows:

	City		Downtown Development Authority	
	<u>Unavailable</u>	<u>Unearned</u>	<u>Unavailable</u>	<u>Unearned</u>
Property taxes	\$ -	\$ 952,184	\$ -	\$ 163,382
Special assessments not yet due (debt service fund)	5,714	-	-	-
Receivables	<u>75,593</u>	<u>35,794</u>	<u>32,213</u>	<u>-</u>
Total deferred/unearned revenue for governmental funds	<u>\$ 81,307</u>	<u>\$ 987,978</u>	<u>\$ 32,213</u>	<u>\$ 163,382</u>

**NOTE G—INTERFUND RECEIVABLES, PAYABLES, AND TRANSFERS**

The composition of interfund balances, caused by normal operation, is as follows:

*Due to/from other funds:*

<u>Receivable fund</u>	<u>Payable fund</u>	<u>Amount</u>
General Fund	Other governmental funds	\$ 338,827
General Fund	Sewer Fund	1,134
General Fund	Water Fund	8,344
General Fund	Water Supply Fund	2,034
Other governmental funds	General Fund	123,991
Other governmental funds	Other governmental funds	152,649
Sewer Fund	Water Fund	81,072
Water Supply Fund	Water Fund	678,339

*Advances from/to primary government and component units:*

<u>Receivable fund</u>	<u>Payable fund</u>	<u>Amount</u>	<u>Purpose</u>
General Fund	Component unit	\$ 10,746	Operational loan
Component unit	Other governmental funds	4,918	Operational loan

Transfers in:

<u>General Fund</u>	<u>Other governmental funds</u>	<u>Total</u>	<u>Purpose</u>
---------------------	---------------------------------	--------------	----------------

*Transfers out:*

General Fund	\$ -	\$ 41,018	\$ 41,018	Debt service
Other governmental funds	40,000	73,519	113,519	Public works
Water Supply Fund	<u>-</u>	<u>24,268</u>	<u>24,268</u>	Recreation
	<u>\$ 40,000</u>	<u>\$ 138,805</u>	<u>\$ 178,805</u>	

City of Muskegon Heights  
**NOTES TO THE FINANCIAL STATEMENTS—CONTINUED**  
December 31, 2004

**NOTE H—LEASES**

The City leases equipment under noncancelable operating leases. Total costs for such leases were approximately \$16,000 for the year ended December 31, 2004. The future minimum lease payments for these leases are as follows:

<u>Year ending December 31</u>	<u>Amount</u>
2005	\$ 13,000
2006	12,500
2007	<u>10,000</u>
	<u>\$ 35,500</u>

**NOTE I—LONG-TERM DEBT**

**Summary of Changes in Long-Term Liabilities**

The following is a summary of long-term liabilities activity for the City for the year ended December 31, 2004.

	<u>Balance January 1, 2004</u>	<u>Additions</u>	<u>Deductions</u>	<u>Balance December 31, 2004</u>	<u>Due within one year</u>
<b>Governmental activities:</b>					
General obligation bonds	\$ 685,000	\$ 1,500,000	\$ 20,000	\$ 2,165,000	\$ 20,000
Capital leases	98,306	-	30,029	68,277	14,000
Installment purchase agreements	192,399	-	96,924	95,475	69,000
Compensated absences	<u>426,305</u>	<u>-</u>	<u>28,791</u>	<u>397,514</u>	<u>110,000</u>
Governmental activity long-term liabilities	<u>\$ 1,402,010</u>	<u>\$ 1,500,000</u>	<u>\$ 175,744</u>	<u>\$ 2,726,266</u>	<u>\$ 213,000</u>
<b>Business-type activities:</b>					
Revenue bonds	<u>\$18,216,799</u>	<u>\$ -</u>	<u>\$ 402,298</u>	<u>\$17,814,501</u>	<u>\$ 420,000</u>
<b>Downtown Development Authority:</b>					
General obligation bonds	\$ 720,000	\$ -	\$ 60,000	\$ 660,000	\$ -
Installment purchase agreements	<u>176,522</u>	<u>-</u>	<u>18,402</u>	<u>158,120</u>	<u>28,500</u>
Downtown Development Authority long-term liabilities	<u>\$ 896,522</u>	<u>\$ -</u>	<u>\$ 78,402</u>	<u>\$ 818,120</u>	<u>\$ 28,500</u>



City of Muskegon Heights  
**NOTES TO THE FINANCIAL STATEMENTS—CONTINUED**  
December 31, 2004

**NOTE I—LONG-TERM DEBT—Continued**

**Summary of Changes in Long-Term Liabilities—Continued**

	Balance December 31, <u>2004</u>
<b>Governmental activities</b>	
<b>General obligation bonds:</b>	
Michigan Municipal Bond Authority, 2004 Financial Stabilization Bonds, due in varying annual installments of \$170,000 to \$210,000 from November 2006 through November 2013, plus interest at 2.5% to 4%	\$ 1,500,000
Michigan Municipal Bond Authority, Series 1997C, Advance Refunding of Series 1991C, Group B of 1991 bonds, due in varying annual installments of \$20,000 to \$75,000 through November 2020, plus interest at 7.2%	665,000
<b>Capital leases:</b>	
6.94% Capital lease payable in quarterly installments of \$4,673 including interest; final payment due March 2009	68,277
<b>Installment purchase agreement:</b>	
4.9% Equipment note payable in total annual installments of approximately \$57,752 plus interest; final payment due December 2005	57,752
4.25% Equipment note payable in current monthly installments of \$1,014 including interest; final payment due April 2008	<u>37,723</u>
	2,328,752
Compensated absences	<u>397,514</u>
	<u>\$ 2,726,266</u>
<b>Business-type activities:</b>	
<b>Revenue bonds:</b>	
Water Supply System revenue bonds of 2000 due in annual installments of \$320,000 to \$1,215,000 through November 2030; plus interest at rates varying from 5.2% to 6.0%	\$17,370,000
Muskegon County wastewater management system no. 1 bond refunding contractual obligation of 1996 final payment due July 2005; plus interest at 5.7%	89,661

City of Muskegon Heights  
**NOTES TO THE FINANCIAL STATEMENTS—CONTINUED**  
December 31, 2004

**NOTE I—LONG-TERM DEBT—Continued**

**Summary of Changes in Long-Term Liabilities—Continued**

	Balance December 31, <u>2004</u>
<b>Business-type activities:—Continued</b>	
<b>Revenue bonds:—Continued</b>	
Muskegon County wastewater management system no. 1 refunding bond of 2002 due in annual installments of \$10,860 to \$115,659 through July 2008; plus interest rates varying from 2.25% to 5%	\$ <u>354,840</u>
	<u>\$17,814,501</u>
<b>Downtown Development Authority:</b>	
<b>General obligation bond:</b>	
\$995,000 Downtown Development limited tax obligation bonds of 1994 due in annual installments of \$50,000 to \$125,000 starting May 2006 through May 2012; plus interest at rates varying from 7.0% to 7.25%	\$ 660,000
<b>Installment purchase agreements:</b>	
Mortgage note payable to bank due in monthly installments of \$2,668 through January 2011; including interest at 9.20%	<u>158,120</u>
	<u>\$ 818,120</u>

The general obligation bonds are backed by the full faith and credit of the City.

The 1996 and 2002 County of Muskegon wastewater contracts payable represent agreements with Muskegon County relating to the construction of sewage treatment facilities. To construct these facilities, the County issued bonds which local municipalities are obligated to repay. The City has recorded the liability for its portion of the County bonds which are to be repaid by the access rights fee. Access rights are also recorded and are amortized over 10 years. The contractual obligation is secured by the full faith and credit of the City. Current debt service requirements are funded by sewer revenues.

The 1996 and 2002 County of Muskegon wastewater contracts payable and the 2000 Water Supply revenue bonds are payable solely from the net revenues of the sewer and water supply directing the City to create funds restricted for use in the construction project and in debt service. Assets so restricted are detailed in note C3.

The City was in compliance in all material respects with all the revenue bond ordinances at December 31, 2004.

City of Muskegon Heights  
**NOTES TO THE FINANCIAL STATEMENTS—CONTINUED**  
December 31, 2004

**NOTE I—LONG-TERM DEBT—Continued**

**Summary of Changes in Long-Term Liabilities—Continued**  
**Downtown Development Authority:—Continued**

Annual debt service requirements to maturity for debt outstanding as of December 31, 2004 follows:

Year ending December 31	Governmental Activities		Business-type Activities		Downtown Development Authority	
	Principal	Interest	Principal	Interest	Principal	Interest
2005	\$ 103,000	\$ 92,282	\$ 420,000	\$ 989,158	\$ 28,500	\$ 60,304
2006	216,395	93,565	451,180	964,237	70,934	56,717
2007	228,154	85,717	469,573	940,895	97,947	50,290
2008	221,623	78,349	483,748	919,291	110,155	42,404
2009	219,580	71,051	390,000	894,293	127,575	33,366
2010-2014	980,000	230,598	2,285,000	4,141,916	383,009	42,560
2015-2018	285,000	67,594	2,990,000	3,433,534	-	-
2019-2023	75,000	-	3,940,000	2,484,563	-	-
2024-2028	-	-	5,170,000	1,245,937	-	-
2029-2030	-	-	1,215,000	68,344	-	-
Total	\$ <u>2,328,752</u>	\$ <u>719,156</u>	\$ <u>17,814,501</u>	\$ <u>16,082,168</u>	\$ <u>818,120</u>	\$ <u>285,641</u>

**NOTE J—OTHER INFORMATION**

**1. Risk Management**

The City is exposed to various risks of loss related to torts; theft of, damage to and destruction of assets; errors and omissions; and natural disasters for which the government carries commercial insurance. Liabilities are reported when it is probable that a loss has occurred and the amount of the loss in excess of insurance coverage can be reasonably estimated. There has been no loss in excess of insurance in the past three years.

**2. Contingent Liabilities**

Amounts received or receivable from grant agencies are subject to audit and adjustment by grantor agencies, principally the federal government. Any disallowed claims, including amounts already collected, may constitute a liability to the applicable funds. The amount, if any, of expenditures that may be disallowed by the grantor cannot be determined at this time, although the City expects such amounts, if any, to be immaterial.

The City is a defendant in various lawsuits. Although the outcome of these lawsuits is not presently determinable, in the opinion of the City's counsel the resolution of these matters will not have a material adverse effect on the financial condition of the City.

The City has had its payroll tax records for the calendar years ended December 31, 2003 and 2004 reviewed by the Internal Revenue Service (IRS). There is the possibility that the City may owe additional payroll taxes, as much as \$25,000 for each of these years. Their review has not been completed nor has the City been issued any specific determinations. It is also possible that the IRS will review other calendar years and additional taxes may be assessed.

City of Muskegon Heights  
**NOTES TO THE FINANCIAL STATEMENTS—CONTINUED**  
December 31, 2004

**NOTE J—OTHER INFORMATION—Continued**

**3. Post-Retirement Health Care**

The City has agreed to provide post-retirement health care to certain full-time employees after they reach age 50 or 55, depending on which contract they are employed under, and have 25 years of service. The City will pay 100 percent of the employee's premium and a portion of the dependent's premium, if any.

As of year end, there were 83 retired employees receiving benefits. The City finances the Plan on a pay-as-you-go basis. For the year ended December 31, 2004, the City's post-retirement health care cost under the Plan was approximately \$401,000.

**NOTE K—EMPLOYEE RETIREMENT SYSTEMS AND PENSION PLANS**

**1. Pension Plan**

*Plan Description.* The City of Muskegon Heights is in an agent multiple-employer defined benefit pension plan with the Municipal Employees Retirement System (MERS). The Plan provides retirement and disability benefits, annual cost-of-living adjustments, and death benefits to Plan members and beneficiaries. Act No. 427 of the Public Acts of 1984 of the State of Michigan assigns the authority to establish and amend the benefit provisions of the plans that participate in MERS to the respective employer entities; that authority rests with the City of Muskegon Heights. A copy of the complete financial report and required supplemental information can be obtained by writing to:

City of Muskegon Heights  
2724 Peck Street  
Muskegon Heights, MI 49444

*Funding Policy.* City employees are required to contribute 3 to 6 percent to the Plan depending on employee contract. The City is required to contribute at an actuarially-determined rate depending upon position from 0.0 to 11.6 percent of covered wages.

*Annual Pension Cost.* For the year ended December 31, 2004, the City's annual pension cost was approximately \$101,000 which the City contributed. The required contribution was determined as part of the December 31, 2003 actuarial valuation using the entry age actuarial cost method. The actuarial assumptions included (a) 8 percent investment rate of return (net of administrative expenses), (b) projected salary increases ranging from 0 percent to 4.5 percent, and (c) 4.5 percent per year compounded annually attributable to inflation. The actuarial value of plan assets was determined using techniques that smooth the effects of short-term volatility in the market value of investments over a five-year period.

City of Muskegon Heights  
**NOTES TO THE FINANCIAL STATEMENTS—CONTINUED**  
December 31, 2004

**NOTE K—EMPLOYEE RETIREMENT SYSTEMS AND PENSION PLANS—Continued**

**1. Pension Plan—Continued**

*Annual Pension Cost—Continued*

<b>Three-Year Trend Information</b>			
<u>Year ending</u>	<u>Approximate Annual Pension Cost (APC)</u>	<u>Percent of APC contributed</u>	<u>Net Pension Obligation</u>
6/30/02	\$20,000	100%	\$ -
6/30/03	39,000	100	-
6/30/04	44,000	100	-

**REQUIRED SUPPLEMENTARY INFORMATION**  
*Schedule of Funding Progress*

*(Dollars amounts in thousands)*

<u>Actuarial valuation date</u>	<u>Actuarial value of assets</u>	<u>Actuarial Accrued Liability (AAL) Entry Age</u>	<u>Unfunded AAL (UAAL)</u>	<u>Funded ratio</u>	<u>Covered payroll</u>	<u>UAAL as a percentage of covered payroll</u>
12/31/01	\$27,226	\$25,709	\$(1,517)	106%	\$4,158	(36.5)%
12/31/02	26,469	26,353	(116)	100	4,225	(2.7)
12/31/03	26,825	27,868	1,043	96	3,982	26.2

**2. Deferred Compensation Plan**

The City offers its employees a deferred compensation plan created in accordance with Internal Revenue Code Section 457. The Plan, available to all full-time City employees at their option, permits participants to defer a portion of their salary until future years. The deferred compensation is not available to participants until termination, retirement, death, or unforeseeable emergency.

The Plan has created a trust for the exclusive benefit of the Plan's participants and beneficiaries under rules provided in Internal Revenue Code Section 401(f).

**NOTE L—ECONOMIC DEPENDENCY**

State of Michigan shared revenues represent 32 percent of General Fund revenues.

The City's Water Supply Fund has a significant economic dependence on two other municipalities that are major users of water services. During the year ended December 31, 2004, the municipality's billings for water usage approximated 67 percent of total billings in the Water Supply Fund.

City of Muskegon Heights  
**NOTES TO THE FINANCIAL STATEMENTS—CONTINUED**  
December 31, 2004

**NOTE M—EQUITY RESTATEMENT**

The General Fund fund balance and net assets were restated effective January 1, 2004. The fund balance and net assets were restated to reflect an additional receivable for income taxes.

The net assets of the governmental activities were also restated to reflect an adjustment to the beginning accumulated depreciation related to the capital assets.

	General Fund <u>fund deficit</u>	Governmental activities <u>net assets</u>
Original balance at January 1, 2004	\$ (938,843)	\$ 9,301,168
Taxes receivable adjustment	114,380	114,380
Accumulated depreciation adjustment	<u>-</u>	<u>40,935</u>
	\$ <u>(824,463)</u>	\$ <u>9,456,483</u>

The Downtown Development Authority net assets were restated lower due to the effect of an additional due to other governmental units of \$92,337 that was not properly recorded.

Net assets at January 1, 2004	\$ 262,421
Due to other government units	<u>(92,337)</u>
Net assets at January 1, 2004, restated	\$ <u>170,084</u>

**NOTE N—SUBSEQUENT EVENT**

Effective January 1, 2005, the wastewater service agreement between the County of Muskegon and thirteen local units, including the City, was amended to provide financial relief to the County's largest industrial user. Under terms of the amendment, the allocation of debt service charged to each local unit user will increase. The Sewer Fund's total debt obligation and annual payments on that obligation will increase by about 21 percent. The estimated additional debt assumed by the City was approximately \$93,000. Additional County wastewater debt is paid by local unit users through user charges based on metered sewage flows. This increase will result in approximately \$26,000 in additional costs in 2005.

The City also entered into a construction in April 2005. This commitment is for street repaving of approximately \$138,000. This contract will be funded through a special assessment.

## **REQUIRED SUPPLEMENTAL INFORMATION**

City of Muskegon Heights  
**REQUIRED SUPPLEMENTAL INFORMATION**  
**BUDGETARY COMPARISON SCHEDULE**  
General Fund  
For the year ended December 31, 2004

	Original budget	Final budget	Actual	Variance with final budget- positive (negative)
<b>REVENUES</b>				
Taxes	\$ 3,009,000	\$ 2,875,000	\$ 2,954,574	\$ 79,574
Licenses and permits	115,000	119,900	110,712	(9,188)
Intergovernmental revenues				
Federal	135,000	157,788	133,873	(23,915)
State	1,840,182	1,924,900	1,892,754	(32,146)
Charges for services	755,900	672,900	764,917	92,017
Fines and forfeitures	10,000	10,000	15,571	5,571
Investment earnings	3,500	4,000	18,600	14,600
Miscellaneous	154,500	154,375	133,255	(21,120)
Total revenues	6,023,082	5,918,863	6,024,256	105,393
<b>EXPENDITURES</b>				
<b>Current</b>				
General government				
City council	\$ 52,334	\$ 32,806	\$ 30,442	\$ 2,364
Mayor	21,007	17,705	17,107	598
City manager	161,496	156,305	154,987	1,318
Personnel	9,300	4,750	5,138	(388)
Elections	11,200	10,700	10,561	139
Income tax	53,069	61,757	57,397	4,360
Assessor	123,788	123,788	126,623	(2,835)
City attorney	95,000	150,000	142,376	7,624
City clerk	59,673	74,898	56,880	18,018
Finance	142,271	144,972	145,871	(899)
Treasurer	49,967	53,028	50,177	2,851
Centennial Celebration	-	5,100	5,100	-
Data processing	11,500	11,500	8,659	2,841
Building and grounds	152,598	184,998	185,384	(386)
Other general government	777,997	862,267	876,288	(14,021)
Motor pool	65,000	70,000	74,267	(4,267)
Public safety				
Police	2,003,280	2,115,619	1,990,764	124,855
Auto theft grant	70,242	70,242	58,826	11,416
Fire	975,209	974,099	988,582	(14,483)
Inspections	219,554	202,335	196,087	6,248
Special investigations	-	3,039	3,046	(7)



City of Muskegon Heights  
**REQUIRED SUPPLEMENTAL INFORMATION**  
**BUDGETARY COMPARISON SCHEDULE—CONTINUED**  
General Fund  
For the year ended December 31, 2004

	Original budget	Final budget	Actual	Variance with final budget- positive (negative)
Public works				
Public works	\$ 52,100	\$ 52,100	\$ 55,835	\$ (3,735)
Street lighting	200,000	180,000	158,821	21,179
Traffic	18,645	12,900	22,025	(9,125)
Refuse collection	500,000	500,000	491,815	8,185
Community and economic development				
Farmer's market	2,500	3,400	3,626	(226)
Planning	2,250	8,800	9,695	(895)
Culture and recreation				
Parks	147,625	165,884	147,918	17,966
Library	26,500	29,325	25,938	3,387
Mona Lake boat launch	-	9,000	8,754	246
Debt service				
Principal	13,840	13,840	26,957	(13,117)
Interest and fees	2,440	2,440	2,540	(100)
Capital outlay	6,500	126,500	156,678	(30,178)
Total expenditures	<u>6,026,885</u>	<u>6,434,097</u>	<u>6,295,164</u>	<u>138,933</u>
Excess (deficiency) of revenues over expenditures	(3,803)	(515,234)	(270,908)	244,326
OTHER FINANCING SOURCES (USES)				
Proceeds from debt issue	-	1,400,000	1,448,269	48,269
Proceeds from sale of capital assets	35,000	35,000	27,016	(7,984)
Transfers in	-	-	40,000	40,000
Transfers out	-	-	(41,018)	(41,018)
Total other financing sources (uses)	<u>35,000</u>	<u>1,435,000</u>	<u>1,474,267</u>	<u>39,267</u>
Net change in fund balances	<u>\$ 31,197</u>	<u>\$ 919,766</u>	1,203,359	<u>\$ 283,593</u>
Fund deficit at January 1, 2004, restated			<u>(824,463)</u>	
Fund balance at December 31, 2004			<u>\$ 378,896</u>	

## **OTHER SUPPLEMENTAL INFORMATION**

City of Muskegon Heights  
BALANCE SHEET  
Other Governmental Funds  
December 31, 2004

	Total other governmental funds	Special Revenue Funds							Debt Service	Permanent Fund Cemetery Perpetual Care
		Major Streets	Local Streets	Community Development Block Grant	Cemetery	Michigan State Housing Development	Recreation	Capital Projects		
ASSETS										
Cash and investments	\$ 667,916	\$ 17,666	\$ 37,904	\$ 25,077	\$ (34)	\$ 7,510	\$ 531	\$ 71,355	\$ 1,270	\$ 506,637
Receivables										
Special assessments	5,714	504	5,210	-	-	-	-	-	-	-
Property taxes	8,752	-	-	-	-	-	8,752	-	-	-
Other	54,508	-	-	-	46,907	-	-	-	-	7,601
Due from other funds	276,640	-	156,041	-	16,232	16,127	85,183	-	3,057	-
Due from other governmental units	201,343	93,881	35,722	71,740	-	-	-	-	-	-
Total assets	<u>\$ 1,214,873</u>	<u>\$ 112,051</u>	<u>\$ 234,877</u>	<u>\$ 96,817</u>	<u>\$ 63,105</u>	<u>\$ 23,637</u>	<u>\$ 94,466</u>	<u>\$ 71,355</u>	<u>\$ 4,327</u>	<u>\$ 514,238</u>
LIABILITIES AND FUND BALANCES (DEFICITS)										
Liabilities										
Accounts payable	\$ 56,648	\$ 28,525	\$ 2,215	\$ 2,914	\$ 4,910	\$ -	\$ 12,662	\$ 5,422	\$ -	\$ -
Accrued liabilities	8,568	3,196	1,075	2,424	1,439	-	434	-	-	-
Customer deposits	2,075	-	-	-	-	-	2,075	-	-	-
Due to other funds	491,476	230,228	41,608	67,699	71,743	23,637	329	40,000	-	16,232
Due to component unit	4,918	-	-	4,036	-	-	-	-	-	882
Deferred revenue	53,129	504	5,210	19,744	-	-	27,671	-	-	-
Total liabilities	616,814	262,453	50,108	96,817	78,092	23,637	43,171	45,422	-	17,114
Fund balances (deficits)										
Reserved for:										
Debt service	4,327	-	-	-	-	-	-	-	4,327	-
Capital projects	25,933	-	-	-	-	-	-	25,933	-	-
Perpetual care	497,124	-	-	-	-	-	-	-	-	497,124
Unreserved										
Special revenue funds	70,675	(150,402)	184,769	-	(14,987)	-	51,295	-	-	-
Total fund balances (deficits)	598,059	(150,402)	184,769	-	(14,987)	-	51,295	25,933	4,327	497,124
Total liabilities and fund balances (deficits)	<u>\$ 1,214,873</u>	<u>\$ 112,051</u>	<u>\$ 234,877</u>	<u>\$ 96,817</u>	<u>\$ 63,105</u>	<u>\$ 23,637</u>	<u>\$ 94,466</u>	<u>\$ 71,355</u>	<u>\$ 4,327</u>	<u>\$ 514,238</u>

City of Muskegon Heights  
**STATEMENT OF REVENUES, EXPENDITURES AND CHANGES IN FUND BALANCES (DEFICITS)**  
 Governmental Funds  
 For the year ended December 31, 2004

		Special Revenue Funds								Permanent Fund
	Total other governmental funds	Major Streets	Local Streets	Community Development Block Grant	Cemetery	Michigan State Housing Development	Recreation	Capital Projects	Debt Service	Cemetery Perpetual Care
REVENUES										
Property taxes	\$ 54,335	\$ -	\$ -	\$ -	\$ -	\$ -	\$ 54,335	\$ -	\$ -	\$ -
Intergovernmental revenues										
Federal	676,330	-	-	676,330	-	-	-	-	-	-
State	942,732	630,901	239,831	-	-	72,000	-	-	-	-
Charges for services	178,940	-	-	-	156,011	-	17,827	-	-	5,102
Investment earnings	20,405	72	3,145	-	600	29	-	122	5	16,432
Other	97,835	349	1,725	29,983	-	-	1,293	64,485	-	-
Total revenues	1,970,577	631,322	244,701	706,313	156,611	72,029	73,455	64,607	5	21,534
EXPENDITURES										
Current										
General government	178,331	-	-	-	178,248	-	-	-	-	83
Public works	702,210	389,273	203,771	-	-	72,070	-	37,096	-	-
Community and economic development	526,261	-	-	526,261	-	-	-	-	-	-
Culture and recreation	107,687	-	-	-	-	-	107,687	-	-	-
Debt service										
Principal	119,996	13,368	-	86,628	-	-	-	-	20,000	-
Interest and fees	57,416	5,323	-	8,989	-	-	-	-	43,104	-
Capital outlay	57,434	7,999	-	49,435	-	-	-	-	-	-
Total expenditures	1,749,335	415,963	203,771	671,313	178,248	72,070	107,687	37,096	63,104	83
Excess of revenues over (under) expenditures	221,242	215,359	40,930	35,000	(21,637)	(41)	(34,232)	27,511	(63,099)	21,451
OTHER FINANCING SOURCES (USES)										
Transfers in	138,805	-	-	-	16,432	-	59,268	-	63,105	-
Transfers out	(113,519)	-	(22,087)	(35,000)	-	-	-	(40,000)	-	(16,432)
Total other financing sources (uses)	25,286	-	(22,087)	(35,000)	16,432	-	59,268	(40,000)	63,105	(16,432)
Net change in fund balances (deficits)	246,528	215,359	18,843	-	(5,205)	(41)	25,036	(12,489)	6	5,019
Fund balances (deficits) at January 1, 2004	351,531	(365,761)	165,926	-	(9,782)	41	26,259	38,422	4,321	492,105
Fund balances (deficits) at December 31, 2004	\$ 598,059	\$ (150,402)	\$ 184,769	\$ -	\$ (14,987)	\$ -	\$ 51,295	\$ 25,933	\$ 4,327	\$ 497,124

City of Muskegon Heights  
Agency Funds  
**COMBINING STATEMENT OF NET ASSETS**  
December 31, 2004

ASSETS

	<u>Combined</u>	<u>Tax Collection</u>	<u>Payroll Imprest</u>	<u>Woodcliffe Village</u>
Cash and investments	\$ 631,974	\$ 548,342	\$ 50,010	\$ 33,622
Accounts receivable	<u>102,712</u>	<u>102,712</u>	<u>-</u>	<u>-</u>
Total assets	<u>\$ 734,686</u>	<u>\$ 651,054</u>	<u>\$ 50,010</u>	<u>\$ 33,622</u>

LIABILITIES

Accounts payable	\$ 103,411	\$ 53,401	\$ 50,010	\$ -
Due to other governmental units	597,653	597,653	-	-
Deposits held for others	<u>33,622</u>	<u>-</u>	<u>-</u>	<u>33,622</u>
Total liabilities	<u>\$ 734,686</u>	<u>\$ 651,054</u>	<u>\$ 50,010</u>	<u>\$ 33,622</u>

City of Muskegon Heights  
**SINGLE AUDIT OF FEDERAL  
FINANCIAL ASSISTANCE PROGRAMS**

Financial Report and  
Independent Auditors' Reports

December 31, 2004

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# BRICKLEY DELONG

CERTIFIED PUBLIC ACCOUNTANTS

## **INDEPENDENT AUDITORS' REPORT ON INTERNAL CONTROL OVER FINANCIAL REPORTING AND ON COMPLIANCE AND OTHER MATTERS BASED ON AN AUDIT OF FINANCIAL STATEMENTS PERFORMED IN ACCORDANCE WITH *GOVERNMENT AUDITING STANDARDS***

June 28, 2005

City Council  
City of Muskegon Heights  
Muskegon Heights, Michigan

We have audited the financial statements of the City of Muskegon Heights as of and for the year ended December 31, 2004 and have issued our report thereon dated June 28, 2005. We conducted our audit in accordance with auditing standards generally accepted in the United States of America and the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States.

### ***Internal Control Over Financial Reporting***

In planning and performing our audit, we considered the City of Muskegon Heights's internal control over financial reporting in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control over financial reporting. However, we noted certain matters involving the internal control over financial reporting and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over financial reporting that, in our judgment, could adversely affect the City of Muskegon Heights's ability to record, process, summarize and report financial data consistent with the assertions of management in the financial statements. Reportable conditions are described as Findings 1-12 in Part B of the accompanying Schedule of Findings and Questioned Costs.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that misstatements caused by error or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over financial reporting would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, of the reportable conditions described above, we consider Finding 1 in Part B of the accompanying Schedule of Findings and Questioned Costs to be a material weakness.



City Council  
June 28, 2005  
Page 2

***Compliance***

As part of obtaining reasonable assurance about whether the City of Muskegon Heights's financial statements are free of material misstatement, we performed tests of its compliance with certain provisions of laws, regulations, contracts, and grants, noncompliance with which could have a direct and material effect on the determination of financial statement amounts. However, providing an opinion on compliance with those provisions was not an objective of our audit and, accordingly, we do not express such an opinion. The results of our tests disclosed no instances of noncompliance or other matters that are required to be reported under *Government Auditing Standards*.

This report is intended solely for the information of the City Council, management, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

*Brickley DeLong, PLC*

# BRICKLEY DELONG

CERTIFIED PUBLIC ACCOUNTANTS

## INDEPENDENT AUDITORS' REPORT ON COMPLIANCE WITH REQUIREMENTS APPLICABLE TO EACH MAJOR PROGRAM AND INTERNAL CONTROL OVER COMPLIANCE IN ACCORDANCE WITH OMB CIRCULAR A-133

June 28, 2005

City Council  
City of Muskegon Heights  
Muskegon Heights, Michigan

### *Compliance*

We have audited the compliance of the City of Muskegon Heights with the types of compliance requirements described in the U.S. Office of Management and Budget (OMB) Circular A-133 *Compliance Supplement* that are applicable to its major federal program for the year ended December 31, 2004. The City of Muskegon Heights's major federal program is identified in the Summary of Auditors' Results section of the accompanying Schedule of Findings and Questioned Costs. Compliance with the requirements of laws, regulations, contracts, and grants applicable to its major federal program is the responsibility of the City of Muskegon Heights's management. Our responsibility is to express an opinion on the City of Muskegon Heights's compliance based on our audit.

We conducted our audit of compliance in accordance with auditing standards generally accepted in the United States of America; the standards applicable to financial audits contained in *Government Auditing Standards* issued by the Comptroller General of the United States; and OMB Circular A-133, *Audits of States, Local Governments, and Non-Profit Organizations*. Those standards and OMB Circular A-133 require that we plan and perform the audit to obtain reasonable assurance about whether noncompliance with the types of compliance requirements referred to above that could have a direct and material effect on a major federal program occurred. An audit includes examining, on a test basis, evidence about the City of Muskegon Heights's compliance with those requirements and performing such other procedures as we considered necessary in the circumstances. We believe that our audit provides a reasonable basis for our opinion. Our audit does not provide a legal determination on the City of Muskegon Heights's compliance with those requirements.

City Council  
June 28, 2005  
Page 2

As described in Findings 13-16 in Part C of the accompanying Schedule of Findings and Questioned Costs, the City of Muskegon Heights did not comply with requirements regarding financial reporting, activities allowed and allowable, procurement, and special tests and provisions for rehabilitation compliance requirements that are applicable to its U.S. Department of Housing and Urban Development Community Development Block Grant Program. Compliance with such requirements is necessary, in our opinion, for the City of Muskegon Heights to comply with requirements applicable to that program.

In our opinion, except for noncompliance described in the preceding paragraph, the City of Muskegon Heights complied, in all material respects, with the requirements referred to above that are applicable to its major federal program for the year ended December 31, 2004.

***Internal Control Over Compliance***

The management of the City of Muskegon Heights is responsible for establishing and maintaining effective internal control over compliance with requirements of laws, regulations, contracts, and grants applicable to federal programs. In planning and performing our audit, we considered the City of Muskegon Heights's internal control over compliance with requirements that could have a direct and material effect on a major federal program in order to determine our auditing procedures for the purpose of expressing our opinion on compliance and to test and report on internal control over compliance in accordance with OMB Circular A-133.

We noted certain matters involving the internal control over compliance and its operation that we consider to be reportable conditions. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control over compliance that, in our judgment, could adversely affect the City of Muskegon Heights's ability to administer a major federal program in accordance with applicable requirements of laws, regulations, contracts, and grants. The reportable conditions are described as Findings 1, 3, 7 and 12 in Part C of the accompanying Schedule of Findings and Questioned Costs.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that noncompliance with the applicable requirements of laws, regulations, contracts, and grants caused by error or fraud that would be material in relation to a major federal program being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions. Our consideration of the internal control over compliance would not necessarily disclose all matters in the internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses. However, of the reportable conditions described above, we consider Finding 1 in Part C of the accompanying Schedule of Findings and Questioned Costs to be a material weakness.

City Council  
June 28, 2005  
Page 3

***Schedule of Expenditures of Federal Awards***

We have audited the financial statements of the City of Muskegon Heights as of and for the year ended December 31, 2004 and have issued our report thereon dated June 28, 2005. Our audit was performed for the purpose of forming an opinion on the financial statements taken as a whole. The accompanying Schedule of Expenditures of Federal Awards is presented for purposes of additional analysis as required by OMB Circular A-133 and is not a required part of the financial statements. Such information has been subjected to the auditing procedures applied in the audit of the financial statements and, in our opinion, is fairly stated, in all material respects, in relation to the financial statements taken as a whole.

This report is intended solely for the information of the City Council, management, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

*Brickley DeLong, PLC*

City of Muskegon Heights  
**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**  
For the year ended December 31, 2004

Federal grantor/pass-through grantor/program title	Federal CFDA number	Entitlement program or award amount	Accrued (deferred) revenue January 1, 2004	Cash or payments in kind received (cash basis)	Amount of grant expenditures	Accrued (deferred) revenue December 31, 2004
<b><i>U.S. Department of Housing and Urban Development</i></b>						
Direct programs						
Community Development Block Grant	14.218					
B-01-MC-26-0027		\$ 586,000	\$ 43,888	\$ -	\$ -	\$ 43,888
B-02-MC-26-0027		593,000	27,148	-	-	27,148
B-03-MC-26-0027		579,000	48,622	426,799	378,177	-
B-04-MC-26-0027		569,000	-	298,152	298,152	-
Program Income		<u>49,727</u>	<u>-</u>	<u>49,727</u>	<u>29,984</u>	<u>(19,743)</u>
Total U.S. Department of Housing and Urban Development		2,376,727	119,658	774,678	706,313	51,293
<b><i>U.S. Department of Justice</i></b>						
Direct programs						
Local Law Enforcement Block Grant Program	16.592					
2003-LB-BX-2807		16,653	-	16,653	16,653	-
2004-LB-BX-1241		<u>11,871</u>	<u>-</u>	<u>11,871</u>	<u>-</u>	<u>(11,871)</u>
		28,524	-	28,524	16,653	(11,871)
Passed through County of Ottawa						
WEMET Multi-Jurisdictional Drug and Gang Task Force	16.579					
70834-503B		<u>24,893</u>	<u>-</u>	<u>9,282</u>	<u>9,282</u>	<u>-</u>
Total U.S. Department of Justice		53,417	-	37,806	25,935	(11,871)
<b><i>U.S. Federal Emergency Management Administration</i></b>						
Direct programs						
Assistance to firefighters grant training program	83.554					
EMW-2003-FG-00326		\$ 112,117	\$ -	\$ 112,117	\$ 107,938	\$ (4,179)

City of Muskegon Heights  
**SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS—CONTINUED**  
For the year ended December 31, 2004

<u>Federal grantor/pass-through grantor/program title</u>	<u>Federal CFDA number</u>	<u>Entitlement program or award amount</u>	<u>Accrued (deferred) revenue January 1, 2004</u>	<u>Cash or payments in kind received (cash basis)</u>	<u>Amount of grant expenditures</u>	<u>Accrued (deferred) revenue December 31, 2004</u>
<i>U.S. Department of Commerce Economic Development Administration</i>						
Direct programs						
Economic Development - Support for planning	11.302					
06-86-04609		\$ 62,400	\$ 2,400	\$ 2,400	\$ -	\$ -
TOTAL FEDERAL ASSISTANCE		<u>\$ 2,604,661</u>	<u>\$ 122,058</u>	<u>\$ 927,001</u>	<u>\$ 840,186</u>	<u>\$ 35,243</u>

**Notes:**

1. See the financial statements footnotes for accounting policies used in preparing this schedule.

City of Muskegon Heights  
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS**  
Year ended December 31, 2004

**A. SUMMARY OF AUDITORS' RESULTS**

1. The auditors' report expresses an unqualified opinion on the financial statements of the City of Muskegon Heights.
2. **Twelve (12)** reportable conditions disclosed during the audit of the financial statements are reported in the Independent Auditors' Report on Compliance and on Internal Control over Financial Reporting Based on an Audit of Financial Statements Performed in Accordance with *Government Auditing Standards* and are reported in Part B of this schedule. **One (1)** of these reportable conditions is reported as a material weakness.
3. There were **no** instances of noncompliance material to the financial statements of the City of Muskegon Heights disclosed during the audit, as reported in Part B of this Schedule.
4. **Four (4)** reportable conditions disclosed during the audit of the major federal award program are reported in the Independent Auditors' Report on Compliance with Requirements Applicable to Each Major Program and Internal Control over Compliance in Accordance with OMB Circular A-133 and are reported in Parts B and C of this schedule. One of the conditions is reported as a material weakness.
5. The auditors' report on compliance for the major federal award program for the City of Muskegon Heights expresses a qualified opinion.
6. Audit findings that are required to be reported in accordance with Section 510(a) of OMB Circular A-133 are reported in this schedule.
7. The program tested as a major program was:

<u>Name</u>	<u>CFDA Number</u>
<i>U.S. Department of Housing and Urban Development</i> Community Development Block Grant	14.218

8. The threshold for distinguishing Types A and B programs was \$300,000.
9. The City of Muskegon Heights was not determined to be a low-risk auditee.

City of Muskegon Heights  
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS—CONTINUED**  
Year ended December 31, 2004

<b>B. FINDINGS RELATING TO THE FINANCIAL STATEMENTS, WHICH ARE REQUIRED TO BE REPORTED IN ACCORDANCE WITH GAGAS</b>	<u>Questioned Costs</u>
<b>COMPLIANCE</b>	
NONE	None
<b>REPORTABLE CONDITIONS</b>	
<b>Year 2004 Finding No. 1: MATERIAL WEAKNESS—Segregation of Duties</b>	
<i>Condition:</i> Due to staff reductions in the accounting department, one individual has multiple responsibilities among several functions causing a lack of segregation of duties.	
<i>Effect:</i> Errors or the misappropriation of funds can go undetected.	None
<i>Recommendation:</i> Internal control procedures should be further segregated.	
<b>Year 2004 Finding No. 2: Investment Reconciliation Procedures</b>	
<i>Condition:</i> During detailed testing, we noted that some investment accounts did not agree with general ledger balances.	
<i>Effect:</i> Investment account balances were incorrectly stated on interim financial statements.	None
<i>Recommendation:</i> The investment accounts should be reconciled to the general ledger on a monthly basis.	
<b>Year 2004 Finding No. 3: Compliance With Federal Grant Agreements</b>	
<i>Condition:</i> During our testing, we noted that the City did not comply with certain federal requirements, as described in Findings 13-16 below.	
<i>Effect:</i> The City could be subject to questioned costs or sanctions.	None
<i>Recommendation:</i> Federal programs should be periodically reviewed to ensure compliance with grant agreements.	
<b>Year 2004 Finding No. 4: Budget Procedures</b>	
<i>Condition:</i> During our testing, we noted that expenditures exceeded appropriations in various funds and departments.	
<i>Effect:</i> The City was not in compliance with Michigan Public Act 621.	None
<i>Recommendation:</i> The budget should be amended as necessary to comply with Michigan Public Act 621.	



City of Muskegon Heights  
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS—CONTINUED**  
Year ended December 31, 2004

**B. FINDINGS RELATING TO THE FINANCIAL STATEMENTS,  
WHICH ARE REQUIRED TO BE REPORTED IN ACCORDANCE  
WITH GAGAS**

Questioned  
Costs

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**REPORTABLE CONDITIONS—Continued**

**Year 2004 Finding No. 5: Street Fund Rental Procedures**

*Condition:* During our testing, we noted that Major Street Fund and Local Street Fund equipment rental schedules were not fully completed.

*Effect:* There could be inaccuracies in equipment rental expense amounts and allocations. None

*Recommendation:* The City should maintain complete and accurate Major Street Fund and Local Street Fund equipment rental schedules.

**Year 2004 Finding No. 6: State Tax Increment Financing Plan  
Reporting Procedures**

*Condition:* During our testing, we noted City personnel inaccurately calculated the amount of school property taxes that the Downtown Development Authority (DDA) was allowed to capture.

*Effect:* The City could overcapture or undercapture DDA property taxes. None

*Recommendation:* The City should establish procedures to ensure the accurate preparation of State of Michigan Tax Increment Financing Plan report.

**Year 2004 Finding No. 7: CDBG Budgeting Procedures**

*Condition:* The City budgeted 2004 CDBG expenditures equal to the federally approved grant. However, the grant spans multiple years with only a portion of the grant to be spent in any given year.

*Effect:* The budgeted 2004 CDBG expenditures are significantly different than would be expected. None

*Recommendation:* The CDBG operating budget should be based upon anticipated expenditures during the year.

**Year 2005 Finding No. 8: Property Tax Collection Fund Cash  
Collections and Disbursements Reconciliation Procedures**

*Condition:* The Property Tax Collection Fund cash collections and disbursements were not reconciled with supporting documents during the year.

*Effect:* Errors or the misappropriation of funds could go undetected during the year. None

*Recommendation:* Property Tax Collection Fund cash collections and disbursements should be reconciled with supporting documents on an interim basis.

City of Muskegon Heights  
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS—CONTINUED**  
Year ended December 31, 2004

**B. FINDINGS RELATING TO THE FINANCIAL STATEMENTS,  
WHICH ARE REQUIRED TO BE REPORTED IN ACCORDANCE  
WITH GAGAS**

Questioned  
Costs

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**REPORTABLE CONDITIONS—Continued**

**Year 2004 Finding No. 9: Reconciliation of Account Balances to  
Supporting Documentation**

*Condition:* General ledger account balances for receivables, interfund receivables/payables, interfund transfers, accounts payable, other liability, and other accounts were not reconciled to supporting documentation on a timely basis.

*Effect:* Failure to reconcile general ledger account balances timely can adversely affect the accuracy of internally-prepared monthly financial statements and, correspondingly, adversely affect the analysis and conclusions as to the City's financial position and results of operations by the City Council, management, and other users of such monthly financial statements. Additionally, this condition significantly increases the amount of year end general ledger account analysis and adjusting journal entries by City personnel, causing significant delays in closing fiscal year financial records and issuing audited financial statements.

*Recommendation:* Account balances should be reconciled to detailed supporting documentation on a timely basis.

None

**Year 2004 Finding No. 10: Water Supply Fund Revenue Recording**

*Condition:* Revenues were not properly recorded in the Water Supply Fund during the year ended December 31, 2004. The Water Supply Fund revenues were incorrectly recorded as revenues in the Water Fund.

*Effect:* This condition resulted in the accounting records reporting the Water Supply Fund with a large current year operating deficit throughout the year ended December 31, 2004.

*Recommendation:* The Water Supply Fund revenues should be recorded monthly in the proper fund.

None

**Year 2004 Finding No. 11: Utility Accounts Receivable Reconciliations**

*Condition:* The general ledger balances for accounts receivable within the utility departments for customers did not agree with the customer detail report.

*Effect:* Failure to timely reconcile accounts receivable general ledger account balances with detailed customer accounts balance creates an opportunity for errors or misappropriations of funds to go undetected.

*Recommendation:* The general ledger and customer detail of utility billing accounts receivable should be reconciled monthly.

None

City of Muskegon Heights  
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS—CONTINUED**  
Year ended December 31, 2004

**B. FINDINGS RELATING TO THE FINANCIAL STATEMENTS,  
WHICH ARE REQUIRED TO BE REPORTED IN ACCORDANCE  
WITH GAGAS**

Questioned  
Costs

---

**REPORTABLE CONDITIONS—Continued**

**Year 2004 Finding No. 12: Federal Financial Reporting Procedures**

*Condition:* There were numerous inaccuracies in the annual U.S. Department of Housing and Urban Development Consolidated Annual Performance Report (CAPER), primarily due to inaccuracies in the City's accounting records.

*Effect:* The CAPER incorrectly reported grant operations.

None

*Recommendation:* Federal program expenditure reports should be filed with accurate financial information.

**C. FINDINGS AND QUESTIONED COSTS—MAJOR FEDERAL  
AWARD PROGRAMS AUDIT**

**COMPLIANCE**

**U.S. Department of Housing and Urban Development**

**Year 2004 Finding No. 13: Financial Reporting on the IDIS**

CFDA: 14.218

Award No.: B-03-MC-26-0027

Award Year Ended: June 30, 2004

*Condition:* Actual expenditures incurred during the year for a couple of grant categories did not agree to the annual U.S. Department of Housing and Urban Development Consolidated Annual Performance Report (CAPER).

*Effect:* The CAPER incorrectly reported grant operations.

None

*Recommendation:* Procedures should be developed to ensure federal reports are accurately prepared.

**U.S. Department of Housing and Urban Development**

**Year 2004 Finding No. 14: Activities Allowed or Allowable**

CFDA: 14.218

Award No.: B-03-MC-26-0027 and B-04-  
MC26-0027

Award Year Ended: June 30, 2004

*Condition:* The procedures utilized to determine income eligibility for individuals applying for the down payment assistance program were inaccurate. City personnel subtracted \$750 per household member from household income before determining if the household qualified for the program.

City of Muskegon Heights  
**SCHEDULE OF FINDINGS AND QUESTIONED COSTS—CONTINUED**  
Year ended December 31, 2004

**C. FINDINGS AND QUESTIONED COSTS—MAJOR FEDERAL  
AWARD PROGRAMS AUDIT**

**COMPLIANCE—Continued**

**U.S. Department of Housing and Urban Development  
Year 2004 Finding No. 14:—Continued**

*Effect:* This reduction in household income could result in services being performed for individual household which did not qualify for the program.

Not  
determinable

*Recommendation:* The City should revise its procedures to comply with federal guidelines.

**U.S. Department of Housing and Urban Development  
Year 2004 Finding No. 15: Procurement**

CFDA: 14.218

Award No.: B-03-MC-26-0027 and B-04-MC-  
26-0027

Award Year Ended: June 30, 2004

*Condition:* The City accepted the highest bid for a project and did not document why the other bids were not utilized.

*Effect:* The program may incur unnecessary expenditures.

Not  
determinable

*Recommendation:* The City should document the rationale in all cases when the lowest bid is not utilized.

**U.S. Department of Housing and Urban Development  
Year 2004 Finding No. 16: Special Tests and Provisions  
(Rehabilitation)**

CFDA: 14.218

Award No.: B-03-MC-26-0027 and B-04-MV-  
26-0027

Award Year Ended: June 30, 2004

*Condition:* Several project files were missing pre-rehabilitation inspections as required by the U.S. Department of Housing and Urban Development.

*Effect:* The City may inadvertently omit rehabilitation items or they might perform un-required services

None

*Recommendation:* The City should complete a pre-rehabilitation inspection for each project and document this inspection with a pre-rehabilitation checklist.

**REPORTABLE CONDITIONS**

See Findings 1, 3, 7 and 12 in Part B above.

None

## **SUPPLEMENTAL INFORMATION**

# BRICKLEY DELONG

CERTIFIED PUBLIC ACCOUNTANTS

## INDEPENDENT AUDITORS' REPORT ON SUPPLEMENTAL INFORMATION

June 28, 2005

City Council  
City of Muskegon Heights  
Muskegon Heights, Michigan

We have audited the financial statements of the City of Muskegon Heights as of and for the year ended December 31, 2004 and have issued our report thereon dated June 28, 2005. Our audit was made primarily for the purpose of forming an opinion on the financial statements taken as a whole. The supplemental information presented on page 18 is provided for purposes of additional analysis and is not a required part of the financial statements or the accompanying Schedule of Expenditures of Federal Awards. Such supplemental information has been subjected to the auditing procedures applied in the audit of the financial statements of the City of Muskegon Heights and, in our opinion, is fairly stated in all material respects in relation to the financial statements taken as a whole.

*Brickley DeLong, PLC*

City of Muskegon Heights  
**SCHEDULE OF RECONCILIATION OF REVENUES FROM FEDERAL SOURCES  
PER FINANCIAL STATEMENTS AND EXPENDITURES PER SINGLE AUDIT  
REPORT SCHEDULE OF EXPENDITURES OF FEDERAL AWARDS**  
For the Year ended December 31, 2004

The following is a reconciliation of federal revenues as reported on page 7 of the City of Muskegon Heights financial statements for the year ended December 31, 2004 and federal expenditures per the Schedule of Expenditures of Federal Awards on page 9 of this single audit report.

Federal revenues per City of Muskegon Heights financial statements  
for the year ended December 31, 2004 (page 7)

General Fund	\$ 133,873
Other governmental funds	676,330
	<u>810,203</u>

Plus program income	29,984
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Rounding variance	<u>(1)</u>
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Federal assistance expenditures and operating transfers out per Schedule of Expenditures of Federal Awards (page 9)	<u><u>\$ 840,186</u></u>
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## **CLIENT DOCUMENTS**



# CITY OF MUSKEGON HEIGHTS

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2724 Peck Street  
Muskegon Heights, MI 49443-0536  
Phone: (231) 733-8870

## SUMMARY SCHEDULE OF PRIOR AUDIT FINDINGS

June 28, 2005

Department of Housing and Urban Development  
Detroit, Michigan

The City of Muskegon Heights respectfully submits the following summary of the current status of prior audit findings contained in the single audit report for the year ended December 31, 2003 dated July 28, 2004.

### B. FINDINGS—FINANCIAL STATEMENT AUDIT

#### COMPLIANCE

There were *no* compliance findings relative to the financial statements.

#### REPORTABLE CONDITIONS

**Year 2003 Finding No. 1: *MATERIAL WEAKNESS***—Assessment of Current Financial Position as of and for the year ended December 31, 2003

*Condition:* The City had significant fund deficits and/or deficit operations for the General Fund and other significant funds.

*Recommendation:* The City Council and management should immediately assess the City's current financial position and forecast the City's 2004 and future operations.

*Current Status:* *No* similar finding was reported in the single audit report for the year ended December 31, 2004.

**B. FINDINGS—FINANCIAL STATEMENT AUDIT—Continued**

**REPORTABLE CONDITIONS—Continued**

**Year 2003 Finding No. 2: MATERIAL WEAKNESS—Payroll Segregation of Duties**

*Condition:* One individual is responsible for numerous payroll and general ledger functions.

*Recommendation:* The segregation of duties within the payroll function should be improved.

*Current Status:* See Finding No. 1 in the Schedule of Findings and Questioned Costs for the year ended December 31, 2004 for a similar finding.

**Year 2003 Finding No. 3: MATERIAL WEAKNESS—General Ledger Journal Entry Review Procedures**

*Condition:* A significant number of journal entries are being posted to the general ledger without review and approval by an appropriate official.

*Recommendation:* Journal entries should be reviewed by an appropriate official.

*Current Status:* No similar finding was reported in the single audit report for the year ended December 31, 2004.

**Year 2003 Finding No. 4: MATERIAL WEAKNESS—Monthly Internal Financial Statements**

*Condition:* City management did not provide internally-prepared financial statements on a monthly basis to the City Council and/or its Finance Committee.

*Recommendation:* Fully-adjusted financial statements, including budget-to-actual comparisons, should be provided timely on a monthly basis to the City Council and/or its Finance Committee.

*Current Status:* No similar finding was reported in the single audit report for the year ended December 31, 2004.

**Year 2003 Finding No. 5: MATERIAL WEAKNESS—Bank Reconciliation Procedures**

*Condition:* Bank reconciliations were not prepared on a timely basis.

*Recommendation:* Bank reconciliations should be prepared on a timely basis.

*Current Status:* No similar finding was reported in the single audit report for the year ended December 31, 2004.

## **B. FINDINGS—FINANCIAL STATEMENT AUDIT—Continued**

### **REPORTABLE CONDITIONS—Continued**

#### **Year 2003 Finding No. 6: Retirement Plan Remittance Procedures**

*Condition:* Certain pension plan contributions were not remitted timely to the plan investment agent within federal requirements.

*Recommendation:* Retirement plan contributions should be remitted on a timely basis.

*Current Status:* *No* similar finding was reported in the single audit report for the year ended December 31, 2004.

#### **Year 2003 Finding No. 7: CDBG Budgeting Procedures**

*Condition:* The City budgeted 2003 CDBG expenditures equal to the federally approved grant. However, the grant spans multiple years with only a portion of the grant to be spent in any given year.

*Recommendation:* The CDBG operating budget should be based upon anticipated expenditures during the year.

*Current Status:* See Finding No. 7 in the Schedule of Findings and Questioned Costs for the year ended December 31, 2004 for a similar finding noted.

#### **Year 2003 Finding No. 8: Property Tax Collection Fund Cash Collections and Disbursements Reconciliation Procedures**

*Condition:* The Property Tax Collection Fund cash collections and disbursements were not reconciled with supporting documents during the year.

*Recommendation:* Property Tax Collection Fund cash collections and disbursements should be reconciled with supporting documents on an interim basis.

*Current Status:* See Finding No. 8 in the Schedule of Findings and Questioned Costs for the year ended December 31, 2004 for a similar finding noted.

#### **Year 2003 Finding No. 9: Property Tax Revenue and Recording Allocation Procedures**

*Condition:* Property tax revenues are recorded as cash is received.

*Recommendation:* Property tax revenues should be allocated and recorded monthly among various funds.

*Current Status:* *No* similar finding was reported in the single audit report for the year ended December 31, 2004.

**B. FINDINGS—FINANCIAL STATEMENT AUDIT—Continued**

**REPORTABLE CONDITIONS—Continued**

**Year 2003 Finding No. 10: Property Tax Collection Fund Remittance Procedures**

*Condition:* The City failed to remit all property taxes which it collected a number of years ago for other governmental units.

*Recommendation:* The Property Tax Collection Fund should pay all amounts owed to other governmental units.

*Current Status:* **No** similar finding was reported in the single audit report for the year ended December 31, 2004.

**Year 2003 Finding No. 11: Monthly General Ledger Closing Procedures**

*Condition:* A significant number of general ledger accounts required numerous adjusting journal entries to correct account activity during the year.

*Recommendation:* The accounting department should utilize a monthly closing checklist in conjunction with the preparation of monthly financial statements.

*Current Status:* **No** similar finding was reported in the single audit report for the year ended December 31, 2004.

**Year 2003 Finding No. 12: Federal Expenditure Reporting Procedures**

*Condition:* There were delays between the time certain federal expenditures were incurred and the request/drawdown of federal funds was performed.

*Recommendation:* The system for tracking grant reimbursement requests and budget amendments of federal programs should be improved.

*Current Status:* **No** similar finding was reported in the single audit report for the year ended December 31, 2004.

**Year 2003 Finding No. 13: Interfund Transfer Recording Procedures**

*Condition:* Several interfund transfers were not recorded in the general ledger during the year.

*Recommendation:* A system should be developed to ensure that all interfund transfers are recorded on a timely basis.

*Current Status:* **No** similar finding was reported in the single audit report for the year ended December 31, 2004.

**B. FINDINGS—FINANCIAL STATEMENT AUDIT—Continued**

**REPORTABLE CONDITIONS—Continued**

**Year 2003 Finding No. 14:** Reconciliation of Account Balances to Supporting Documentation

*Condition:* General ledger account balances for receivables, interfund receivables/payables, interfund transfers, accounts payable, other liability, and other accounts were not reconciled to supporting documentation on a timely basis.

*Recommendation:* Account balances should be reconciled to detailed supporting documentation on a timely basis.

*Current Status:* See Finding No. 9 in the Schedule of Findings and Questioned Costs for the year ended December 31, 2004 for a similar finding noted.

**Year 2003 Finding No. 15:** Monitoring Accounts Receivable and Grants Receivable

*Condition:* Some accounts receivable and grants receivable balances were delinquent in excess of a year.

*Recommendation:* Accounts receivable and grants receivable balances should be reviewed periodically.

*Current Status:* No similar finding was reported in the single audit report for the year ended December 31, 2004.

**Year 2003 Finding No. 16:** Interfund Obligations

*Condition:* Several funds have maintained significant interfund liability balances while cash balances were available to satisfy significant portions of the liabilities.

*Recommendation:* Due to/due from other funds accounts should be monitored and cleared in a timely manner.

*Current Status:* No similar finding was reported in the single audit report for the year ended December 31, 2004.

**Year 2003 Finding No. 17:** Water Fund Revenue Recording

*Condition:* No revenues were recorded in the Water Supply Fund during the year ended December 31, 2003. The Water Supply Fund revenues were incorrectly recorded as revenues in the Water Fund.

*Recommendation:* The Water Supply Fund revenues should be recorded monthly in the proper fund.

*Current Status:* See Finding No. 10 in the Schedule of Findings and Questioned Costs for the year ended December 31, 2004 for a similar finding noted.

## **B. FINDINGS—FINANCIAL STATEMENT AUDIT—Continued**

### **REPORTABLE CONDITIONS—Continued**

#### **Year 2003 Finding No. 18: Utility Accounts Receivable Reconciliations**

*Condition:* The general ledger balances for accounts receivable within the utility departments for customers did not agree with the customer detail report.

*Recommendation:* The general ledger and customer detail of utility billing accounts receivable should be reconciled monthly.

*Current Status:* See Finding No. 11 in the Schedule of Findings and Questioned Costs for the year ended December 31, 2004 for a similar finding noted.

#### **Year 2003 Finding No. 19: Federal Financial Reporting Procedures**

*Condition:* There were numerous inaccuracies in the annual U.S. Department of Housing and Urban Development Consolidated Annual Performance Report (CAPER), primarily due to inaccuracies in the City's accounting records.

*Recommendation:* Federal program expenditure reports should be filed with accurate financial information.

*Current Status:* See Finding No. 12 in the Schedule of Findings and Questioned Costs for the year ended December 31, 2004 for a similar finding noted.

## **C. FINDINGS—MAJOR FEDERAL AWARD PROGRAMS**

### **COMPLIANCE**

#### **U.S. Department of Housing and Urban Development**

##### **Year 2003 Finding No. 20: Financial Reporting on the IDIS**

CFDA: 14.218

Award Year Ended: June 30, 2003

*Condition:* The City made multiple budget amendments on the federal Integrated Disbursement and Information System (IDIS), while not maintaining reconciliations of the effects of such amendments. Further, supporting documentation for expenditures reported on IDIS was not readily available.

*Recommendation:* See Finding No. 13 in Part B above.

*Current Status:* See Finding No. 13 in the Schedule of Findings and Questioned Costs for the year ended December 31, 2004 for a similar finding noted.

Department of Housing and Urban Development  
June 28, 2005  
Page 6

**C. FINDINGS—MAJOR FEDERAL AWARD PROGRAMS—Continued**

**COMPLIANCE**

**U.S. Department of Housing and Urban Development**

**Year 2003 Finding No. 21:** Financial Reporting on the IDIS

CFDA: 14.218

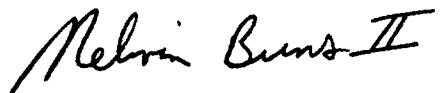
Award Year Ended: June 30, 2003

See Finding No. 19 in Part B above.

**REPORTABLE CONDITIONS**

See Findings 12 and 19 in Part B above.

Sincerely,

A handwritten signature in black ink that reads "Melvin Burns II". The signature is written in a cursive, flowing style.

Melvin Burns, II  
City Manager

# CITY OF MUSKEGON HEIGHTS

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2724 Peck Street  
Muskegon Heights, MI 49443-0536  
Phone: (231) 733-8870

## CORRECTIVE ACTION PLAN

June 28, 2005

Department of Housing and Urban Development  
Detroit, Michigan

The City of Muskegon Heights respectfully submits the following Corrective Action Plan for the year ended December 31, 2004.

Name and address of independent public accounting firm:

Brickley DeLong, PLC  
P.O. Box 999  
Muskegon, Michigan 49443

Audit period: December 31, 2004

The findings from the Schedule of Findings and Questioned Costs for the year ended December 31, 2004 are discussed below. The findings are numbered consistently with the numbers assigned in the schedule. Section A of the schedule, Summary of Auditors' Results, does not include findings and is not addressed.

## B. FINDINGS—FINANCIAL STATEMENT AUDIT

### COMPLIANCE

There were *no* compliance findings in relation to the financial statements.

### REPORTABLE CONDITIONS

#### **Year 2004 Finding No. 1:** Segregation of Duties

*Recommendation:* Internal controls should be further segregated.

*Management Response:* City staff understands the need for this recommendation. With its limited staff, we will continue to examine opportunities to further segregate responsibilities or provide oversight and review of various functions.



## **B. FINDINGS—FINANCIAL STATEMENT AUDIT—Continued**

### **REPORTABLE CONDITIONS—Continued**

#### **Year 2004 Finding No. 2: Investment Reconciliation Procedures**

*Recommendation:* The investment accounts should be reconciled to the general ledger on a monthly basis.

*Management Response:* City staff acknowledges the need to consistently reconcile these accounts on a monthly basis. While no misappropriations have occurred, it is a practice that will be consistently implemented.

#### **Year 2004 Finding No. 3: Compliance With Federal Grant Agreements**

*Recommendation:* Federal programs should be periodically reviewed to ensure compliance with grant agreements.

*Management Response:* Upon knowledge of this finding, City staff will be performing a complete review of its compliance procedures and initiate a self-monitoring review. Several department directives have been issued with respect to this recommendation and others will be initiated as necessary.

#### **Year 2004 Finding No. 4: Budget Procedures**

*Recommendation:* The budget should be amended as necessary to comply with Michigan Public Act 621.

*Management Response:* City staff attempts to estimate all year end final expenditures so that Council can make year end amendments to appropriations. City staff will more closely monitor all year end expenditures and commitment in order to accurately make year end budget amendments.

#### **Year 2004 Finding No. 5: Street Fund Rental Procedures**

*Recommendation:* The City should maintain complete and accurate Major Street Fund and Local Street Fund equipment rental schedules.

*Management Response:* The City has used and updated these schedules consistently in the past. A change in key personnel resulted in this not being completed for the entire year. It has been done for the prior year. The appropriate staff has been instructed on the appropriate procedures, and they have been implemented for the current year.

**B. FINDINGS—FINANCIAL STATEMENT AUDIT—Continued**

**REPORTABLE CONDITIONS—Continued**

**Year 2004 Finding No. 6: State Tax Increment Financing Plan Reporting Procedures**

*Recommendation:* The City should establish procedures to ensure the accurate preparation of State of Michigan Tax Increment Financing Plan report.

*Management Response:* This recommendation points out a management oversight. Staff will make the necessary revision to the previous reports and recalculate the amounts that should be captured. Where applicable, the City will orchestrate the appropriate redistribution of taxes.

**Year 2004 Finding No. 7: CDBG Budgeting Procedures**

*Recommendation:* The CDBG operating budget should be based upon anticipated expenditures during the year.

*Management Response:* Management staff had the budget worksheets prepared for inclusion budget after receiving this recommendation last year; however, it was inadvertently omitted in the final budget adoption. The current budget will be amended to address this and notes made in the budget preparation file to insure the recommendation is implemented.

**Year 2004 Finding No. 8: Property Tax Collection Fund Cash Collections and Disbursements Reconciliation Procedures**

*Recommendation:* Property Tax Collection Fund cash collections and disbursements should be reconciled with supporting documents on an interim basis.

*Management Response:* Management acknowledges the purpose and intent of this recommendation and has committed to the consistent and accurate documenting of the current year.

**Year 2004 Finding No. 9: Reconciliation of Account Balances to Supporting Documentation**

*Recommendation:* Account balances should be reconciled to detailed supporting documentation on a timely basis.

*Management Response:* Improvements have been made with respect to this recommendation. Staff will continue to work on improving the timeliness of balancing all accounts.

**B. FINDINGS—FINANCIAL STATEMENT AUDIT—Continued**

**REPORTABLE CONDITIONS—Continued**

**Year 2004 Finding No. 10: Water Fund Revenue Recording**

*Recommendation:* The Water Supply Fund revenues should be recorded monthly in the proper fund.

*Management Response:* While this recommendation has not been implemented completely, staff has consulted with an outside firm and had them assist in addressing this recommendation. Additional computer software and upgrades have been acquired and should reduce the amount of staff time required to comply with this recommendation. We anticipate significant improvement in the current fiscal year.

**Year 2004 Finding No. 11: Utility Accounts Receivable Reconciliations**

*Recommendation:* The general ledger and customer detail of utility billing accounts receivable should be reconciled monthly.

*Management Response:* As stated above, the use of outside accounting assistance and implementation of new computer software should significantly improve our ability to address this recommendation.

**Year 2004 Finding No. 12: Federal Financial Reporting Procedures**

*Recommendation:* Federal program expenditure reports should be filed with accurate financial information.

*Management Response:* This recommendation primarily relates to the CAPER. Staff has made improvement in this reporting and reconciling it to the final audited financial statements. Staff will be working with an outside consultant to refine its process for working with both its internal accounting system and HUD's accounting in order to produce and file completely accurate reports.

## **C. FINDINGS—MAJOR FEDERAL AWARD PROGRAMS**

### **COMPLIANCE**

#### **U.S. Department of Housing and Urban Development**

##### **Year 2004 Finding No. 13:** Financial Reporting on the IDIS

CFDA: 14.218

Award No.: B-03-MC-26-0027

Award Year Ended: June 30, 2004

*Condition:* Actual expenditures incurred during the year for a couple of grant categories did not agree to the annual U.S. Department of Housing and Urban Development Consolidated Annual Performance Report (CAPER).

*Recommendation:* Procedures should be developed to ensure federal reports are accurately prepared.

*Management Response:* City staff will be working with an outside consultant to refine its process for working with both its internal accounting system and HUD's accounting in order to produce this report thoroughly and accurately.

#### **U.S. Department of Housing and Urban Development**

##### **Year 2004 Finding No. 14:** Activities Allowed or Allowable

CFDA: 14.218

Award No.: B-03-MC-26-0027 and B-04-MC26-0027

Award Year Ended: June 30, 2004

*Condition:* The procedures utilized to determine income eligibility for individuals applying for the down payment assistance program were inaccurate. City personnel subtracted \$750 per household member from household income before determining if the household qualified for the program.

*Recommendation:* The City should revise its procedures to comply with federal guidelines.

*Management Response:* This procedure has been revised, and the practice discontinued. This change in procedure will be placed in a department directive and issued to and reviewed with staff.

#### **U.S. Department of Housing and Urban Development**

##### **Year 2004 Finding No. 15:** Procurement

CFDA: 14.218

Award No.: B-03-MC-26-0027 and B-04-MC-26-0027

Award Year Ended: June 30, 2004

*Condition:* The City accepted the highest bid for a project and did not document why the other bids were not utilized.

*Recommendation:* The City should document in all cases when the lowest bid is not utilized.

*Management Response:* Documenting bids not accepted by the lowest bidder is the current practice and procedure used by the City. It was not observed in this case, all staff will be re-advised of this practice. In addition, through City staff self-monitoring and review will attempt to identify any other cases where this may not have occurred.

**C. FINDINGS—MAJOR FEDERAL AWARD PROGRAMS—Continued**

**COMPLIANCE—Continued**

**U.S. Department of Housing and Urban Development**

**Year 2004 Finding No. 16:** Special tests and provisions (Rehabilitation)

CFDA: 14.218

Award No.: B-03-MC-26-0027 and B-04-MV-26-0027

Award Year Ended: June 30, 2004

*Condition:* Several project files were missing pre-rehabilitation inspections as required by the U.S. Department of Housing and Urban Development.

*Recommendation:* The City should complete a pre-rehabilitation inspection for each project and document this inspection with a pre-rehabilitation checklist.

*Management Response:* To ensure complete compliance with this regulation, City staff will be issued a directive that restates this requirement and revises the case documents to include this item on a checklist.

**REPORTABLE CONDITIONS**

See Findings 1, 3, 7 and 12 in Part B above.

If the Department of Housing and Urban Development has questions regarding this plan, please call Melvin Burns, II at (231) 733-8870.

Sincerely,

A handwritten signature in black ink that reads "Melvin Burns II". The signature is written in a cursive, flowing style.

Melvin Burns, II  
City Manager

# BRICKLEY DELONG

CERTIFIED PUBLIC ACCOUNTANTS

June 28, 2005

City Council  
City of Muskegon Heights  
Muskegon Heights, Michigan

In planning and performing our audit of the financial statements of the City of Muskegon Heights for the year ended December 31, 2004, we considered its internal control in order to determine our auditing procedures for the purpose of expressing our opinion on the financial statements and not to provide assurance on the internal control. However, we noted certain matters involving internal control and its operation that we consider to be reportable conditions under standards established by the American Institute of Certified Public Accountants. Reportable conditions involve matters coming to our attention relating to significant deficiencies in the design or operation of the internal control that, in our judgment, could adversely affect the City of Muskegon Heights' ability to initiate, record, process and report financial data consistent with the assertions of management in the financial statements. We have attached a summary of such reportable conditions.

A material weakness is a reportable condition in which the design or operation of one or more of the internal control components does not reduce to a relatively low level the risk that errors or fraud in amounts that would be material in relation to the financial statements being audited may occur and not be detected within a timely period by employees in the normal course of performing their assigned functions.

Our consideration of internal control would not necessarily disclose all matters in internal control that might be reportable conditions and, accordingly, would not necessarily disclose all reportable conditions that are also considered to be material weaknesses as defined above. We believe that the recommendations in the Material Weaknesses section of the attached summary are material weaknesses.

This report is intended for the information and use of the City Council, management, and federal awarding agencies and pass-through entities and is not intended to be and should not be used by anyone other than these specified parties.

## **REPORTABLE CONDITIONS**

The reportable conditions summarized below are categorized within two groups: material weaknesses and other reportable conditions. Within each of these two categories, the reportable conditions are divided between those noted during the December 31, 2004 audit and those noted during the December 31, 2003, 2002 and 2001 audits.

### **MATERIAL WEAKNESSES**

Recommendation 1: Internal control procedures should be further segregated.

The City reduced staff in the accounting department during the last fiscal year. The reduction in staffing has resulted in a lack of segregation of duties within the accounting department. The City currently has the same person performing the payroll function, cash disbursement function and bank reconciliations. Organizations with limited resources and personnel inherently have difficulty in establishing and maintaining an accounting system with strong internal accounting controls including significant segregation of duties.

City management should continue using its current accounting systems, but should seek opportunities to further segregate duties and strengthen internal controls. Often, the most effective approach is the expansion of documented approval of transactions by personnel outside of the accounting department and the segregation of responsibilities of those executing transactions and those with oversight, accounting, and reconciling functions.

### **OTHER REPORTABLE CONDITIONS**

Recommendation 2: The investment accounts should be reconciled to the general ledger on a monthly basis.

During our testing, we noted some investment accounts that did not agree to the general ledger. The investment accounts did not agree due to transactions occurring in the investment account which were not recorded or transactions that were inaccurately recorded in the general ledger.

The timely reconciliation of investment accounts would reduce the possibility of inadvertent errors or misappropriations going undetected.

Recommendation 3: Federal programs should be periodically reviewed to ensure compliance with grant agreements.

During our audit, we noted several findings related to federal compliance requirements. We noted findings related to failure to solicit bids, failure to complete pre-rehab checklists and improper calculation of household income. The City is required to comply with these compliance requirements, along with other federal requirements as part of receiving federal grant monies.

The internal control system related to federal programs should establish, monitor and update procedures to ensure that the City is in compliance with all federal programs requirements.

## OTHER REPORTABLE CONDITIONS—CONTINUED

Recommendation 4: The budget should be amended as necessary to comply with Public Act 621.

During our testing, we noted expenditures exceeded appropriations in various funds and departments. The budget is the authorization by the City Council to incur expenditures, and the budget should be amended prior to incurring expenditures beyond appropriations.

The proper amending of budgets would increase compliance with Public Act 621 and would assist in the maintenance of fiscal discipline.

Recommendation 5: The City should maintain complete and accurate Major Street Fund and Local Street Fund equipment rental schedules.

During our testing, we noted that the Major Street and Local Street equipment rental schedules were not fully completed. The schedules did not include a proper allocation of rental usage by the Major Street Fund. In addition, the schedule did not differentiate between different categories of rental such as routine maintenance and winter maintenance.

The City should maintain the equipment rental schedules on a least a monthly basis. The schedules should include support for each fund and department usage during the month.

Recommendation 6: The City should establish procedures to ensure the accurate preparation of State of Michigan Tax Increment Financing Plan report.

During our testing, we noted City personnel had inaccurately calculated the amount of school property taxes the Downtown Development Authority was allowed to capture. The report was completed inaccurately and utilized out of date debt amortization schedules instead of actual expenditures.

The accurate preparation of the Tax Increment Financing Plan report would reduce the possibility of excess capture of school district property taxes.



## **PRIOR YEAR OTHER REPORTABLE CONDITIONS STILL APPLICABLE**

We consider the following other reportable conditions contained in our July 28, 2004 letter as still applicable:

Recommendation 3: The Community Development Block Grant Fund operating budget should be developed based upon anticipated expenditures during the year.

Recommendation 4: Property Tax Collection Fund cash collections and disbursements should be reconciled with supporting documents on an interim basis.

We consider the following other reportable conditions contained in our November 25, 2002 letter as still applicable:

### ***General***

Recommendation 8: Account balances should be reconciled to detailed supporting documentation on a timely basis.

### ***Utility Billing***

Recommendation 13: The Water Supply Fund revenues and cash collected should be recorded monthly in the proper fund.

Recommendation 14: The general ledger and customer detail of utility billing accounts receivable should be reconciled monthly.

### ***Federal Programs***

Recommendation 15: Federal program expenditure reports should be filed with accurate financial information.